THE FREEMAN

Ideas On Liberty

- The Attack on Concentration
- The Ghost of John D. Rockefeller
- A Peaceful Ferment in Somalia

JUNE 1998

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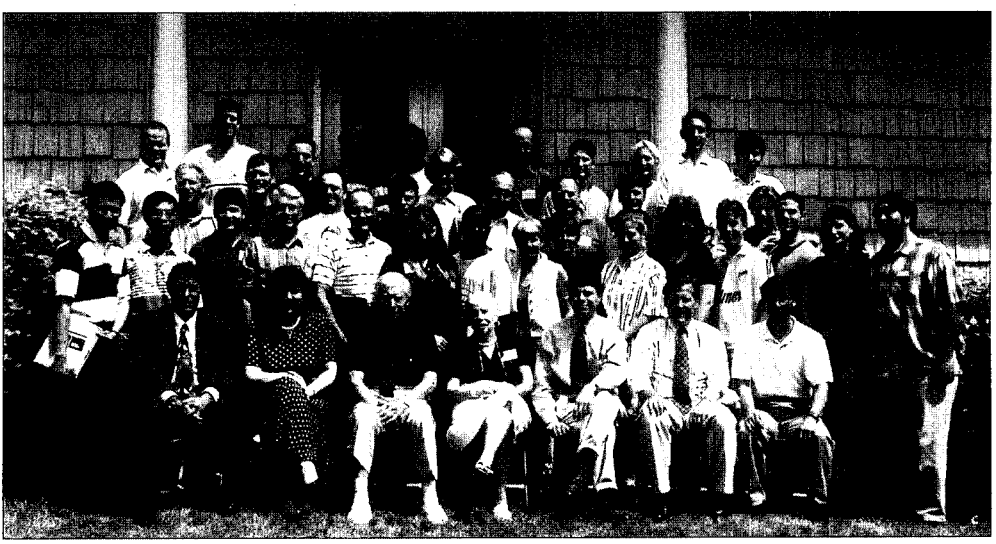

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PERSPECTIVE

Yale Brozen

Good economists do two things. First, they challenge people's intuitions. (Such as: social order requires design; more people mean fewer resources; high market share indicates a lack of competition.) Then they make people say, "Oh, that's simple; I should have thought of that."

By that standard, Yale Brozen, a former member of the University of Chicago Graduate School of Business faculty and the FEE Board of Trustees, qualifies as a very good economist.

Brozen died March 4 at the age of 80. The obituary in the *San Diego Union Tribune* paid him the highest compliment an economist can be paid. It said his "persuasive arguments and tenacious scholarship helped revive widespread acceptance of free-market economics." That aptly describes Yale Brozen. He was part of that revival precisely because he could do what too few economists can: he could write for the non-economist. He did it, among many venues, in the pages of *The Freeman*. In December 1966 he wrote his first *Freeman* article, "Welfare Without the Welfare State." Then in September 1967 he contributed "Rule by Markets Versus Rule by Men." That article was followed by "The Untruth of the Obvious" in June 1968, "The Attack on Concentration" in January 1979, and "The Mythology of Energy" in July 1979.

We are pleased to reprint "The Attack on Concentration" in the present issue. Some of Brozen's most important work was in the area of economics called "industrial organization." Theoretically and empirically, he showed that a high market share for a dominant firm, absent government barriers to entry, was consistent with vigorous competition. With the Department of Justice [sic] persecuting Microsoft for having too many customers for its computer operating system, Brozen's article is as important as ever. Clearly, the attorneys in the department need to learn some economics.

Brozen began teaching business economics in 1957 at the University of Chicago, where he was a colleague of future Nobel laureates

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F.A. Hayek, Milton Friedman, and George Stigler. He was an editorial adviser to *New Individualist Review*, an important early journal of libertarian thought edited by Ralph Raico and Ronald Hamowy at the university. Brozen contributed two articles to *NIR*, "Wage Rates, Minimum Wage Laws, and Unemployment" (Spring 1966) and "The Revival of Traditional Liberalism" (Spring 1965).

In the latter he wrote, "A discussion of the revival of liberalism should begin with a description of what it is—particularly since our latter-day reactionaries have stolen the name. They have stolen the label for a good reason: it stands for the opposite of what they propose. . . . Literally, liberalism meant to liberalize or liberate—to make free—to permit men to do or say whatever they wished. Of course, there was a constraint implied in this. No man could do anything which affected the liberty of others. . . . The classical liberal was and is opposed to all forms of tyranny."

Yale Brozen will be missed.

* * *

David Henderson leads off the issue with a professional and personal appreciation of Yale Brozen, who did not have to be a household name to make a real impact on economic thinking.

Thomas DiLorenzo goes back to the nineteenth century to demonstrate Brozen's point that in a free market, a dominant firm, or "trust," signifies competition, falling prices, and expanded production. The implications for the antitrust laws and the Microsoft case are monumental.

Leonard Read, FEE's founder, liked to remind people that economics is not about numbers but about human action, choices, and values—which makes it a branch of moral philosophy. We reprint his classic article on the subject in our year-long observance of the one hundredth anniversary of his birth.

Civil society is the latest fad interest among academic writers who see a conflict between individual freedom and the "social good." Drawing on the wisdom of an earlier writer, Juliana Geran Pilon believes that resolving the alleged conflict lies in the insight that benevolence is a form of self-love.

Voltaire, that joyous figure of the Enlightenment, visited London early in the eighteenth century. Wandering into the Stock Exchange, writes Wendy McElroy, he beheld the key to England's peace and prosperity.

There is a place on earth where there is no central government, where law arises from custom based on respect for the individual, and where trade today flourishes. Spencer Heath MacCallum will be our tour guide.

Contemplating how the bureaucrats use statistics to justify their meddlesome work, John Wenders sees numbers as the key to government mischief-making. Since they conceal more than reveal, they are the perfect cover for intervention.

Lots of good theory has been penned to demonstrate that government should not build and operate public-works projects, such as railroads and canals. Burton Folsom makes the same point via history, using Stevens T. Mason, a governor of Michigan in the nineteenth century, as an example of a well-intentioned government official who learned that politics and entrepreneurship don't mix.

In "The Pursuit of Happiness," guest columnist Edward Younkins finds a surprising number of movies that portray business activity in a good light. Take this article with you next time you head for the video store. Doug Bandow talks about the budget surplus. Lawrence Reed counsels: In Government Don't You Trust. Dwight Lee looks at the role of incentives in economics. And Mark Skousen traces the intellectual odyssey of a prominent English economic historian.

Our book-review section examines the source of wealth, gun control, the connection between progress and freedom, environmental concerns, free trade, and subsidies to workers.

—SHELDON RICHMAN

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In Memoriam: Yale Brozen

by David R. Henderson

On March 4, at age 80, Yale Brozen, a prominent free-market economist, died. For a large part of his career, Brozen was a professor of business economics at the University of Chicago, where he was a colleague of Nobel prize winners Merton Miller and the late George Stigler and other members of the so-called "Chicago School" such as Lester Telser, Peter Pashigian, Sam Peltzman, and the late Reuben Kessel.

Brozen was one of the nation's leading experts on antitrust laws, and, in virtually all of his writing and speaking on antitrust, was critical of intervention by the antitrust authorities. A typical example was his paper "The Attack on Concentration," which is reprinted in his book *Is Government the Source of Monopoly? and Other Essays*, published by the Cato Institute in 1980. One issue he wrote about in that essay was a Federal Trade Commission complaint against Du Pont. What was Du Pont's alleged crime? That it had "adopted and implemented a plan to expand its domestic production capacity." Brozen commented: "In whatever way I torture the phrases in the antitrust law, I simply cannot get it to say that expanding trade is illegal despite the thunder in the FTC complaint."

Brozen's view of the harm done by antitrust was based on his belief that economies in which governments refrain from creating monopolies are intensely competitive. In Brozen's view, government was the source of virtually all monopolies that were harmful. His clearest statement of that view was his essay "Is Government the Source of Monopoly?" which first appeared in *The Intercollegiate Review*, Winter 1968/69. I still remember my thrill when, at age 18, I read that essay. In it, Brozen makes a detailed empirical case with example upon example of the use of government power to form monopolies. With the possible exception of George Stigler, Brozen did the most to spread that view in the economics profession and in popular writing on economics. His 1975 book, *The Competitive Economy: Selected Readings* (General Learning Press), is a collection of 42 punchy readings by various economists and the best such book I know of. It shows just how intensely competitive an unregulated economy is and how antitrust laws can do damage. One of its best sections includes six articles that refute the idea that predatory pricing is a sensible strategy for firms that would like to have a monopoly.

The dominant view among economists in the field of industrial organization in the 1960s was that industries with a few firms were monopolistic and that this explained why profit rates were higher in concentrated industries than in unconcentrated ones. Harold Demsetz, a former Chicago colleague who moved to UCLA in 1971, dubbed this the "market concentration doctrine." Brozen, with Demsetz, was a modern-day Schumpeterian who saw a dynamic competitive process at work. In industries in which a few

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companies had a large market share, they believed, concentration didn't cause high profits. Rather, concentration and high profits were caused by successful competition. In his 1982 book, *Concentration, Mergers, and Public Policy* (Macmillan), Brozen weaves together evidence from Demsetz and other economists, along with his own findings, to drive home that point.

Interestingly, although Brozen never seemed to come across an antitrust suit he liked (perhaps he just didn't write about those), to my knowledge he was never willing to advocate abolishing antitrust. I believe his hesitancy was due to his acceptance of the "perfectly competitive" model as an ideal. In fact, it was partly to nudge him gently toward abolition that I wrote my preface to his 1980 collection of essays.

But Brozen was much more than a scholar of industrial organization and antitrust. He was also a policy activist, in the best and most honorable sense of that term. In the early 1970s, Brozen noticed that economists around the country were writing solid academic articles critical of much government regulation—of trucking, oil prices, natural-gas prices, and pharmaceuticals, to name four prominent examples. So, as an adjunct scholar with the Washington-based American Enterprise Institute, he gently pushed many of these economists to write rigorous monographs that a general audience could understand. According to Marvin Kosters, director of economic policy studies at AEI, "Yale Brozen contributed more than any other scholar to establishing the credibility of the Institute's research studies in the 1970s."

Major deregulations occurred in oil, natural gas, and trucking within five to eight years of these studies. Often when I ship goods by truck, I silently thank my Hoover colleague Thomas G. Moore for his devastating 1972 study, *Freight Transportation Regulation*, and Yale Brozen for getting him to do it. In fact, as an economist with the Council of Economic Advisers in 1973, I used information from Moore's study to persuade my boss, chairman Herb Stein, to keep the council pushing for transportation deregulation within the Nixon administration.

A memorial note on Yale Brozen is not complete without a reference to his sense of humor, his passion, and his humanity. Yale was a man who liked a good laugh and who cared passionately about his work because he cared about people. I remember the first time I met him, while I was a junior economist in the Nixon White House in the summer of 1973. One of my UCLA professors, George Hilton, was in town and had organized a dinner to which he invited Yale, Ross Eckert (since deceased), and me. We had a great time, laughing about the Washington absurdities we were seeing all around us and exchanging information about how, like McGruff the crime dog, we could take our little bite out of government. At that dinner, Yale encouraged me a lot, as did Hilton, to push for transportation deregulation. Of course, that was also Watergate summer, when the hearings on the scandal were capturing the whole town's attention and Nixon was stonewalling Congress's attempt to make him cough up crucial information. It was also price-control summer, when Nixon's hated economic program (hated by everyone at that dinner, at least) was causing serious shortages of gasoline and many other goods, including with poetic justice, steak in the White House mess. Toward the end of the evening, Eckert, who was also working in the Nixon administration, announced, "Well, gentlemen, I'm leaving. I've got to get up early in the morning and work for my President."

I decided to take a chance. "I'd better leave, too," I announced, grinning. "I've got to get up even earlier to work *against* my President." Yale laughed spontaneously and his eyes twinkled.

From then on I was friends with Yale. I just wish that I had called him sometime in the last five years. I hadn't even known that he had moved to San Diego four years ago. I'm not unusual. While researching this article, I talked to one economist who, after leaving Chicago over 20 years ago, was never again in touch with him even though he liked both Brozen and his work. There's a lesson here. We, especially men, need to break our pattern of isolation and express our appreciation of people before they die. I'm doing way better than I did years ago, and I've still got a long way to go. □

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The Attack on Concentration

by Yale Brozen

(Editor's Note: Yale Brozen, former member of FEE's board of trustees and a retired professor of business economics at the University of Chicago, died March 4. Reprinted below as a memorial is his article published in *The Freeman*, January 1979. It is especially timely because of the government's current legal action against Microsoft.)

Once we gave high regard to those who created great enterprises by designing desirable products, producing them at low cost, and offering them at such attractive prices that they won a large body of customers. Henry Ford, in his day, was looked upon as an industrial hero. Today, he would be regarded as a monopolizing fiend upon whom the antitrust prosecutors should be unleashed. The 1921 Ford Company, with its more than 60 percent share of the market, would today be called a dominant firm and charged with violating the antitrust laws.

Just a few months ago [1978], an antitrust complaint was served upon Du Pont because it developed a low-cost method for producing titanium dioxide pigments. There was no objection to the development of a lower-cost method of production, but Du Pont made the fatal error of passing enough of the cost saving on to buyers to win 40 percent of the market served by domestic producers. Not only did it do that but it is going on to enlarge its capacity, building a new plant at De Lisle, Mississippi, in order to serve even more customers (who also would like to obtain domestic titanium dioxide at low cost). Can you imagine that any enterprise would engage in such a nefarious activity? It should, according to the Federal Trade Commission (FTC), behave like a monopolist. It should restrict its output, instead of expanding, and charge higher prices (and let the business go to foreign firms).

Antitrust Upside Down

That is a total perversion of the intent of our antitrust law. If the FTC is not standing antitrust law on its head, then I simply do not understand what our antitrust law says. The words "every contract, combination, or conspiracy, in restraint of trade is hereby declared to be illegal" say that it is *restraint of output* that is in violation of the law. But the FTC contends that Du Pont is violating the law because it has "adopted and implemented a plan to *expand* its domestic production capacity."[1] That quite plainly says that the FTC regards Du Pont as breaking the law by *expanding* trade. Is that what the law says is illegal?

In whatever way I torture the phrases in the antitrust law, I simply cannot get it to say that expanding trade is illegal despite the thunder in the FTC complaint. Whenever anyone builds more capacity and uses it to produce

This article is condensed from an address before the Ashland, Kentucky, Economic Club, September 15, 1978.

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more product, more trade must result. I can't believe that Du Pont is building a new titanium dioxide plant just because it wants a handsome monument at which to gaze—and neither does the FTC. What the FTC is complaining about is that Du Pont intends to produce titanium dioxide in its new plant and increase its sales—and it is nasty of Du Pont to have already built enough plant to take care of 40 percent of the needs of customers for domestic product. That makes Du Pont "the nation's dominant producer." There can hardly be anything more venal than a "dominant producer," unless it is a "shared monopoly."

"Brand Proliferation" Through Hypnotic Advertising

"Shared monopoly" sounds like a label for a conspiracy among several firms to monopolize a market and share the fruits of that monopoly. But that is not what the FTC means by the label. The phrase is FTC code for a few firms winning and holding a large share of the business in some product line. The FTC staff is currently prosecuting Kellogg, General Foods, and General Mills for "sharing a monopoly" of ready-to-eat (RTE) cereals. These three firms have managed to produce and distribute cereals that taste good enough and cost consumers little enough to win more than three-quarters of the RTE business. That is their crime.

Did these three firms conspire with each other to somehow force other firms out of the industry and then conspire to reduce supplies and raise prices? The FTC disavows any accusation of any such conspiracy. It says that the crime of which these firms are guilty is "brand proliferation." The heinous conduct of which it accuses these firms is that of trying to give consumers what they want. It is now a crime, that is, the FTC is trying to make it a crime, to follow that old merchandising maxim for success, "give the lady what she wants."

The cereal companies should have stuck to producing corn flakes. Never mind the demand for a bran cereal, or a high-protein cereal, or a vitamin-enriched cereal, or a presweetened cereal. Anyway, says the FTC in its complaint, there are no differences between cereals—except those artificially created in the minds of consumers by hypnotizing them with advertising.[2] Of course, if the new brands offered by the three firms in the 1950s and 1960s had not won a large share of the market, nothing would have been wrong with "brand proliferation." But the new brands pleased consumers. They won for the three firms a large share of the market. That, at bottom, is the crime these firms committed. The RTE cereal industry has become "concentrated," that is, most of the sales in the industry are made by a few firms. That is a condition which neither the FTC nor the Antitrust Division intends to tolerate.

The FTC staff also has accused the eight major petroleum refiners of engaging in a "shared monopoly" in the petroleum-refining industry. It is asking that these corporations be broken into smaller companies. The major crime of which the Big Eight stand accused is that of maintaining a "noncompetitive market structure." This phrase is never cogently defined by the FTC staff, but "concentration" seems to be the nub of it. Complaint counsel says the eight companies "are well vertically integrated firms with *substantial horizontal concentration* at every level of the industry" (emphasis supplied).[3] Counsel also says the eight "own and operate refineries accounting for approximately 65 percent of rated crude oil refining capacity in the relevant market." Even more damning, "This figure . . . understates concentration . . . because [the eight firms] . . . utilize more of their refining capacity than other refiners. Hence [their] share of *production* of refined petroleum products . . . is higher than their share of rated refinery capacity. . . ."

Again, here is the accusation that these alleged monopolists are not behaving like monopolists. Instead of restricting output and restraining trade, they push their capacity harder than do their competitors and expand output and trade. Apparently they are unaware of the fact that they are monopolists who can get higher prices by restricting output. Again, the FTC is displeased by efforts to expand trade and is standing antitrust law on its head by saying that the *failure to restrict trade* is a

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violation of the law. The FTC even accuses the companies of building pipelines to provide themselves with "cheap transportation." Again, as in titanium dioxide, it is apparently illegal to reduce costs and pass enough of these cost savings on to customers to win an appreciable share of the market. (In the petroleum case, we cannot say a "large" share of the market has been won since no petroleum-refining firm sells as much as ten percent of the petroleum products sold in the United States.)

These three cases are cited to show the current state of antitrust doctrine at the antitrust agencies. The question remains of whether the courts will buy this upside-down view of antitrust law in view of its legislative history.[4]

Antitrust Not Intended to Fragment Industry

When federal antitrust policy began, with the signing of the Sherman Act in 1890, it was aimed at benefiting consumers. In the words of Senator John Sherman, the act was to outlaw arrangements "designed, or which tend, to advance the cost to the consumer." It was neither intended to fragment industry nor to prevent occupancy of a major share of a market by one or a few firms. When Senator George Hoar explained to the Senate the Judiciary Committee's final draft of the bill, he declared that *a man who "got the whole business because nobody could do it as well as he could" would not be in violation of the Sherman Act.* As Professor Robert Bork has pointed out in his examination of Sherman Act legislative history, "The statute was intended to strike at cartels, horizontal mergers of monopolistic proportions, and predatory business tactics."[5] As the act itself says, "Every conspiracy in *restraint* of trade . . . is hereby declared illegal" (emphasis supplied).

Cost and price reductions and product improvements by a firm expand the trade of a whole industry. Since firms doing this frequently win a large share of the markets in which they operate, judges in the early days of antitrust litigation did not hold "concentration" of sales in the hands of a few firms or "dominance" by a single firm to be illegal in and of itself. Standard Oil and American Tobacco were broken up in 1911 because they had been built by a very large number of mergers of monopolistic proportions with wrongful intent and had then engaged in "acts and dealings wholly inconsistent with the theory that they were made with the single conception of advancing the development of business . . . by usual methods. . . ." The defendants failed to show that the intent underlying their mergers and their acts was the normal one of efficiency and expansion of trade—they failed to show "countervailing circumstances" in Chief Justice Edward White's phrase. They were, therefore, subjected to antitrust remedies. The remedies were not applied because of their dominance but because they were formed and maintained by *monopolizing* acts and intent—that is, by a desire to gain *control* of the supply of a product and to use that control to charge a monopoly price and thereby restrain trade.

Dominant Firms Do Not Control Supply and Price

There is a distinction between *controlling* the supply of a product and *producing* or selling most of the supply of a product. "Dominant" producers who *sell* a major portion of a product's supply usually have no control over the supply. They have no power to set any lower level of industry output and a higher price than that which would prevail in a market with many suppliers and no dominant firm. Usually, a dominant producer is the most efficient firm in the industry. Its large output is the result of its efficiency in supplying the market. The market price is as low as it would be with many producers—frequently lower. Any attempt by a dominant firm to restrict its own supply and increase price after reaching a "dominant" position simply results in the expansion of output by other firms, the entry of additional firms, and loss of its dominance. A dominant firm can keep its dominance only by behaving competitively. *The fact that there is a dominant firm, or small group of firms, in an industry is evidence of competitive behavior—not of monopolization.*

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The lack of ability of a dominant firm (or group of firms) to control supply and price simply because it produces a major part of the supply of a product is illustrated by the experience of the automobile industry in 1927. From 1921 to 1925 the Ford Motor Company supplied more automobiles than all other firms combined. The Ford Company was a dominant firm. It completely shut off its supply to the market for nearly the entire year in 1927 when it closed down to retool for the change from the Model T to the Model A. If the fact that a firm supplies the majority of a market gives it any power to *control* supply and price, then the complete withdrawal of that firm's supply should certainly cause a rise in price. Yet the prices of automobiles failed to rise when Ford shut down despite its having been the dominant producer. Other manufacturers increased their output and prices *fell* by mid-1927 despite the complete withdrawal of the Ford supply of newly manufactured cars from the market.[6]

The fact that a dominant producer has, at most, a very short-lived ability to influence the price of a product can be illustrated by numerous anecdotes. The American Sugar Refining Company merged 98 percent of the capacity for refining sugar east of the Rockies in 1891 and 1892. By cutting production it managed to raise refining margins by 40 percent in 1893 (which raised the price of sugar by 8 percent). Expansion of output in other firms cut sugar-refining margins in 1894 to a level little higher than the 1891 margins despite further reductions in output by American Sugar. By 1894, the entry of additional capacity had forced margins back nearly to 1891 levels and had cut American's share of the sugar business by one-quarter. American was still a dominant firm by today's FTC definition, but it had lost all influence over price and output despite its 85 percent share of capacity.[7]

In 1901, American Can merged 90 percent of all capacity in the can business. It raised prices by one-quarter and lost one-third of its share of market in short order despite additional buying up of competitors and their output. Prices returned to the pre-merger level in a very short time.

These are the most successful monopolizing cases I can find aside from the Air Line Pilots Association, the Teamsters, and similar labor unions.[8] What they demonstrate is that a dominant firm quickly ceases to have any influence in the market if it charges a supracompetitive price. In some cases a dominant firm willing to restrict output greatly has *no* ability to obtain a supracompetitive price even in the short run.

Shifting Market Shares

Dominant firms, that is, firms which sell a major part of all product sold, remain dominant only if they charge the competitive price *and* are more efficient than other firms in their industries. If they are less efficient, they soon find their market share dwindling despite selling at competitive prices. The Big Four in the meatpacking industry, for example, has seen its share of the market dwindle from 56 percent in 1935 (and from an even higher share in earlier years) to 47 percent in 1947 to 38 percent in 1956 to 22 percent in 1972.[9] The relative inefficiency of the Big Four showed in the 1920s when their rates of return on investment ran at one-third the rate earned by smaller companies.[10] That situation continued up to at least 1972, and market share of these inefficient firms fell.

The Big Four meat-packers (the Big Five in the 1917 FTC investigation) originally achieved a large market share in meatpacking by their efficiency—by instituting assembly-line methods with complete utilization of all by-products. They became known for using everything "but the squeal." Also, their development of refrigerated packing houses, cold storage, the refrigerator car, and an efficient distribution system created enlarged markets for meat supplied from cheaper livestock sources. They grew large by being innovative. Once their innovations were imitated by other packers, the decline of the Big Four began, accelerating with the spread of highways and the rise of trucking.

The "dominance" of the Big Four did not give them any power to restrict output or to control price. If anything, the rise of the Big Four decreased the dominance of local mar-

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kets by local butchers who had to compete with fresh meat brought in by train by the Big Four,[11] especially after state laws prohibiting the sale of "foreign" meat were ruled unconstitutional. Nevertheless, the FTC filed one of its earliest "shared monopoly" suits in September 1948 against Armour, Cudahy, Swift, and Wilson, accusing them of "conducting . . . operations . . . along parallel noncompetitive lines." They had served consumers too well, thus incurring the hostility of local butchers in the late nineteenth century and the first quarter of this century. Long after local packers began outcompeting the Big Four, in the second quarter of the century, the FTC, in a flagrantly anticonsumer action, rode to rescue the fair maidens who by now had grown mustaches and larger biceps than the Big Four. The FTC demanded that Armour and Swift each be broken into five companies and that Cudahy and Wilson each be broken into two firms. The FTC reluctantly dropped the suit in March 1954, nearly six years and millions in legal costs after it was brought, but only because the court ruled that pre-1930 behavior was irrelevant in a 1950s proceeding.

Why Are Dominant Firms Being Attacked?

The attacks on concentration whether in the form of an attack on a "dominant" firm or a "shared monopoly," seem to be fairly episodic. The question to be asked is why large firms with a large share of the market are left undisturbed for long periods and then turned on at other times. It is not purely coincidental that the nation suffered a severe deflation from 1882 to 1890, prices dropping by 25 percent in that interval, and the Sherman Act was passed in 1890. At that time, the declining prices were blamed on "cutthroat" and "predatory" competition—and this was also a time in which economies of scale in manufacturing, combined with a rapidly declining cost of transportation, led to centralization of production in enlarged facilities.

From 1867 to 1887, for example, sugar production doubled, from one-half to one million tons annually, and the number of refineries decreased from 60 to 27. In the same period, railroad freight rates fell by 60 percent.[12] The economies of centralized production together with reduced transport costs led to larger plants supplying more distant markets at lower prices than the smaller plants resident in those markets. So the myth of "cutthroat" competition and "predatory" pricing was born in this and many other industries. Antitrust cases were brought against dominant firms such as American Sugar, Standard Oil, American Tobacco, and others.

Another deflation in which prices again dropped by 25 percent, from 1929 to 1933, again led to animus against "Big Business" and especially against that rising innovation in marketing, the chain store. The investigations of the Temporary National Economic Committee once again directed the country's ire toward dominant firms and industrial concentration. Antitrust cases were brought against dominant firms such as Alcoa and A&P and against "shared monopolies" as in the Mother Hubbard case against the petroleum companies, the proceeding against the major cigarette companies, and the FTC case against the Big Four in meatpacking.

Currently, we are trying to find scapegoats for inflation.[13] So we have brought cases against "dominant" firms such as IBM, AT&T, and Du Pont, and against the "shared monopolies" already described.

When we are troubled by deflation or by inflation, both brought on by the government's ineptness in operating our monetary and fiscal policy, the politicians export the blame to somebody else. Mr. Carter tells us in his speeches that the government is not at fault for our inflation—it is up to business and labor to bring inflation to a halt.

In this modern day, we are no longer subject to the kind of superstitions that led the early colonists to hang witches when they were troubled by forces they did not understand. Instead, in this enlightened age, when we seek to rid ourselves of the causes of inflation and other mysterious ailments, we pillory dominant firms or the Big Fours in concentrated, and not so concentrated, industries.

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The Potential Losses from Deconcentration

This absurd behavior by our politicians and its acceptance by the electorate as being something more than a hunt by politicians for witches to blame for their own mistakes might be tolerable if it were nothing more than expensive entertainment of voters. But it is something more. It is counterproductive in terms of the ends we seek—less inflation, higher rates of growth, and improved levels of living.

Prices have gone up less rapidly in our most concentrated industries than in others and productivity has grown more rapidly. From 1967 to 1973, prices in our most concentrated industries rose less than half as rapidly as prices in all manufacturing.[14] From 1958 to 1965, prices in our most concentrated manufacturing industries actually fell while prices in other manufacturing industries rose. Yet it is our concentrated industries with a superior record for moderating inflation and a superb record for increasing productivity that are being cast in the role of economic villains.[15]

If this witch-hunt continues, the result will be economic disaster. If we deconcentrate all our manufacturing industries in which four firms produce and sell more than 50 percent of the product, the result will be a 20 percent rise in costs and a 10 to 15 percent rise in prices.[16] If we want to hasten our decline to the status of a banana republic, the attack on concentration will contribute to that end. □

1. *FTC News Summary*, April 14, 1978, p. 1. Emphasis supplied.
2. FTC Docket No. 8883, April 26, 1972.
3. Complaint Counsel's Prediscovery Statement, In the Matter of Exxon Corporation, et al., Docket No. 8934, pp. 7–10.
4. The Court did accept this upside-down view in reversing the lower court in the Alcoa case. Yale Brozen, "Antitrust Out of Hand," The Conference Board *Record*, vol. 11, no. 3 (March 1974). [The government did not prevail in any of these cases.—Ed.]
5. Robert Bork, *The Antitrust Paradox* (1978), p. 20.
6. Federal Trade Commission, *Report on Motor Vehicle Industry* (Washington, D.C.: U.S. Government Printing Office, 1939).
7. Richard Zerbe, "The American Sugar Refinery Company, 1887–1914; The Story of Monopoly," *Journal of Law & Economics*, vol. 12 (1969), pp. 353–57.
8. Yale Brozen, "The Consequences of Economic Regulation," *New Guard*, vol. 15 (June 1975).
9. The 1956 and subsequent figures overstate the share of market retained by the original Big Four since Cudahy was displaced by Hormel.
10. Ralph C. Epstein, *Industrial Profits in the United States* (New York: National Bureau of Economic Research, 1934), reports that 23 leading meat-packers earned 1.9 percent on equity in 1928 while 46 minor meat-packers earned 10.0 percent. In 1964, leading packers earned 3.7 percent while small packers earned 13.6 percent.
11. Ambrose Winston, "The Chimera of Monopoly," *The Atlantic Monthly* (1924), reprinted in *The Freeman* (September 1960).
12. The average rail rate fell from 19 mills per ton-mile to 7.5 mills.
13. J. Cotlin, "Increased Corporation Antitrust Suits Prompt Industry Fears of New Federal Policy," *National Journal Reports*, September 15, 1973, p. 1371.
14. Steven Lustgarten, *Industrial Concentration and Inflation* (Washington, D.C.: American Enterprise Institute for Public Policy Research, 1975), Table 2.
15. Shirley Scheibla, "Monopoly the Villain," *Barron's*, November 4, 1974, pp. 9, 18–20; "Economic Concentration: The Perennial Fall Guy," First National City Bank *Monthly Economic Letter*, April 1972.
16. Sam Peltzman, "The Gains and Losses from Industrial Concentration," *Journal of Law & Economics*, vol. 20 (October 1977).

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Trust Not in What Your Government Can Do for You

With so much talk these days of scandal, incompetence, and failed programs, trust in government is on the ropes. To some people, this development is lamentable. They are busy writing columns and editorials about the need to "renew our faith in democratic institutions."

But among those who understand the difference between government in the abstract and government in reality—between what America's Founders had in mind and how today's politicians actually behave—declining trust in government evokes a contrasting view: it's richly deserved, long overdue, and we should pray for more of it.

A number of recent polls testify to a fading faith in government. One from the American Enterprise Institute and the Roper Center showed that barely more than 20 percent of Americans "trust government in Washington to do what is right 'most of the time' or 'just about always.'" That's down from about three-quarters of Americans in 1963. (A poll conducted by the Pew Research Center for the People & the Press put the trust figure at 34 percent in February of this year.) A Peter Hart/Robert Teeter survey for the Council on Excellence in Government found that only 8 percent of Americans think the federal government "has enjoyed a large number of successes." The same poll revealed that 47 percent think government "hinders the American Dream."

The National Election Studies (NES) Trust in Government Index tells us that a mere 31 percent of Americans say they trust the government today, about half the 61 percent who said they did in 1966 when the Great Society was getting underway. If only 31 percent had trusted the government then, perhaps we wouldn't have—30 years and endless alphabet programs and agencies later—a $5 trillion national debt with little to show for it but broken families, an eroded currency, and diminished liberties.

To put it bluntly, it's just plain stupid to lament a decline in trust in government until you find out why it's happened. Context is critical here. When the British monarchy was perpetrating "a long train of abuses and usurpations," sending forth "swarms of officers to harass our people and eat out their substance," it was hardly a lamentable fact that American citizens lost faith in King George. They would have had to be deaf, dumb, and generally insensate *not* to lose faith.

America's Founders did not want a government in which the citizens placed blind confidence. Thomas Jefferson was especially noted for his desire to cultivate a healthy distrust of the state. To Abigail Adams in 1787 he wrote, "The spirit of resistance to government is so valuable on certain occasions, that I wish it to be always kept alive. . . . I like a little rebellion now and then. It is like a storm in the atmosphere."

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The steep decline in trust in government since the mid-1960s is proof that large numbers of Americans are awake and learning something. Politicians who promised the sky delivered the proverbial mess of pottage instead. Remember the assurances of how billions of tax dollars siphoned through the federal bureaucracy would solve poverty? The result would be laughable were it not so tragic, so obviously tragic that a president of the same party as Franklin Roosevelt signed a bill in 1996 to end the federal entitlement to public welfare.

If, after the experience of the last 30 years, Americans had lost no faith in government welfare programs, they would likely be diagnosed as possessing a prime symptom of clinical insanity: doing the same harmful thing over and over again and expecting different results each time.

Few if any polls or surveys separate out what people think of the basic, original framework of American *government* from what they think of the characters who are actually doing the *governing*. I suspect that if you asked a cross section of citizens, "Do you trust the concepts embraced by the Declaration of Independence and the Constitution of the United States?" you'd get a higher number than if you asked, "Did you trust Richard Nixon after Watergate?" or "Do you trust Bill Clinton when he says he's faithful to Hillary?"

What's lamentable here is that some of our politicians lie, cheat, and steal. It is *not* lamentable that Americans lose faith in them when they do those things. It is laudable, because it is common sense being appropriately applied.

After all, what does it mean to "trust" someone or something? It means the object of that trust has earned respect and confidence through high standards of reliability, truthfulness, and performance. I can think of no reason why governments deserve your trust any more than anything or anyone else when they fail to meet those standards.

In fact, I can think of a reason why government ought to be held to even higher standards: unlike private individuals or private institutions, it has the legal power to seize your assets whether you trust it or not. If the French political philosopher Pierre-Joseph Proudhon was right (and on this score, I think he was), then it isn't too much for citizens to ask their government to at least be honest with them: "To be governed is to be watched over, inspected, spied on, directed, legislated at, regulated, docketed, indoctrinated, preached at, controlled, assessed, weighed, censored, and ordered about, by men who have neither the right nor the knowledge nor the virtue."

Columnist James Glassman of the American Enterprise Institute, in a February 26 column for the Internet magazine *IntellectualCapital.com*, sees another kind of good news from the latest spate of trust-in-government numbers. People, he says, are beginning to realize that "their happiness is not dependent on what government does. In fact, they are happy *despite* what government does."

Glassman cites the remarkable results of another poll question: "Which statement comes closer to your view: 'The government is responsible for the well-being of all its citizens and it has an obligation to help people when they are in trouble,' or 'People are responsible for their own well-being, and they have an obligation to take care of themselves when they are in trouble.'" In 1983, 43 percent of respondents replied that the government is responsible and 46 percent said people are responsible. In the 1997 poll, however, the results were 16 percent for government, 66 percent for people.

That shift in the years from 1983 to 1997, says Glassman, "is a refreshing development." Unless you like trillions of dollars of debt or you think the Internal Revenue Service is run by Mother Teresa, you have to agree.

If Americans had really lost all faith in the state, however, they would want to take back the responsibility for their retirement years. They would assume the duty of making sure their children are educated. I haven't seen any polls yet that would suggest a majority of Americans are ready for such rugged individualism. So in some respects we could benefit from even further erosion of "trust in government." □

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THE FREEMAN
IDEAS ON LIBERTY

The Ghost of John D. Rockefeller

by Thomas J. DiLorenzo

At the Senate Judiciary Committee hearing on competitiveness in the computer industry last March, Microsoft chairman Bill Gates was compared to the infamous "robber baron" John D. Rockefeller and his company likened to the Standard Oil Company of the late nineteenth century. Federal Trade Commission chairman Robert Pitofsky made a similar analogy in a *Washington Post* op-ed, where he self-servingly argued for more money for antitrust investigations. Gates's competitors, too, are working diligently to implant the Rockefeller analogy in the public consciousness.

Even the *Wall Street Journal* has joined in this attack; reporter Alan Murray claimed in a page-one article that Gates supposedly enjoys "monopoly power" that "even John D. Rockefeller could envy."

Microsoft's critics are right. There are many similarities between Bill Gates's company and the old Standard Oil organization.

Like Gates, Rockefeller was the victim of a political assault for the "sin" of rapid innovation, a vast expansion of output, and rapidly *declining* prices—just the opposite of what the antitrust laws ostensibly police. As with Microsoft, the political attack on Standard Oil was launched by less-efficient rivals who wanted to achieve through the political process what they failed to achieve in the marketplace.

There is indeed a lesson to be learned from Rockefeller's antitrust ordeal, but it is not the one Microsoft's critics have in mind.

Rockefeller's Economic Legacy

The firm of Rockefeller, Andrews, and Flagler was formed in 1865 and was a marvel of efficiency because of Rockefeller's penny-pinching ways and the managerial genius of his brother William.[1] Even Rockefeller's harshest critic, the muckraking journalist Ida Tarbell (whose brother's firm—the Pure Oil Company—was driven from the market by the more efficient Standard Oil), described the company as "a marvelous example of economy."[2]

The efficiencies of economies of scale and vertical integration caused the prices of refined petroleum to fall from over 30 cents a gallon in 1869 to 10 cents by 1874 and to 5.9 cents by 1897. During the same period, Rockefeller reduced his average costs from 3 cents to 0.29 cents per gallon.

The production of refined petroleum *increased* rapidly throughout this period of increasing dominance by Standard Oil as well, as increased competition was provided by Associated Oil and Gas, Texaco, the Gulf Company, and 147 independent refineries that had sprung into existence by 1911—the year in which the government forced the breakup of Standard Oil.

Contrary to popular mythology, Standard Oil's market share *declined* from 88 percent in

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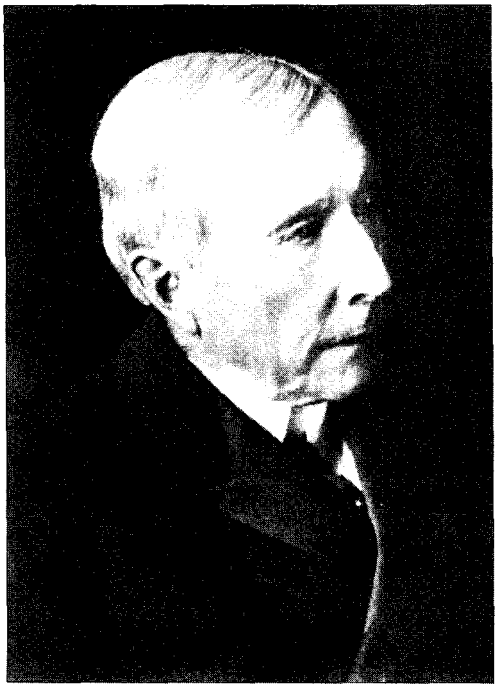

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John D. Rockefeller
(1839–1937)

1890 to 64 percent by 1911. Because of intense competition the company's oil production as a percentage of total market supply had declined to a mere 11 percent in 1911, down from 34 percent in 1898.

Moreover, Standard Oil's decades-long price-cutting was not "predatory pricing"—the theoretical practice of pricing below average cost to drive competitors from the market and establish a monopoly. Any business person would be a fool to intentionally lose money by pricing below average cost *for decades*. As economist John McGee concluded in his classic analysis of the Standard Oil case, "whatever else has been said about [it], the old Standard organization was seldom criticized for making less money when it could readily have made more" through other means.[3]

Indeed, Standard Oil never came close to cornering the market; by the time the antitrust case against it was filed in 1906, it had hundreds of competitors. Nevertheless, Standard Oil was convicted of violating the antitrust laws in 1911 and partially dissolved, despite the fact that the courts conducted no economic analysis of its conduct and performance. That is, they completely ignored the effects the company had on prices, output, and innovation in the petroleum industry, just as Microsoft's critics tend to ignore that there are tens of thousands of software development firms in the world and that during the period of Microsoft's rise to dominance the cost of computing has fallen spectacularly while product quality has soared.

Standard Oil was convicted because of a general anti-business animus stoked by socialist intellectuals and journalists such as Henry Demarest Lloyd and Ida Tarbell and urged on by the company's higher-cost and higher-priced rivals. As a result the most efficient industrial organization of the time was crippled, weakening competition and pushing prices up.

The Protectionist Roots of Antitrust

From the very beginning, the antitrust laws have been a protectionist vehicle. While in theory they guard consumers against monopoly, in reality they politically protect uncompetitive (but well-connected) businesses. In a 1985 *International Review of Law and Economics* article, I showed that in the ten years before the 1890 Sherman Anti-Trust Act, the industries accused of being "monopolized" by trusts were all *dropping* their prices faster than the general price level was falling at that time and were *expanding* output faster than GNP was growing—some as much as ten times faster.[4] The late-nineteenth-century trusts were the most innovative and fastest-growing industries of their time, which is why they were unfairly targeted by antitrust laws.

Indeed, Congress at the time recognized the great advantages of the trusts *for consumers*. Congressman William Mason stated during the U.S. House of Representatives debate over the Sherman Act that the "trusts have made products cheaper, have reduced prices; but if the price of oil, for instance, were reduced to one cent a barrel, it would not right the wrong done to the people of this country by the 'trusts' which have destroyed legitimate competition and driven honest men from legitimate business enterprises."[5] Senator George F. Edmunds

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Bill Gates

added that "Although for the time being the sugar trust has perhaps reduced the price of sugar, and the oil trust certainly has reduced the price of oil immensely, that does not alter the wrong of the principle of any trust."[6]

Thus, members of Congress acknowledged that the trusts had caused lower prices to the great benefit of consumers, but objected that higher-priced businesses—many of which were political supporters—had lost market share or had been driven out of business.

The Sherman Act was a protectionist scheme in more ways than one. The real source of monopoly power in the late nineteenth century was government intervention. In October 1890, just three months after the Sherman Act was passed, Congress passed the McKinley tariff—the largest tariff increase in history up to that point. The bill was sponsored by none other than Senator John Sherman himself. Sherman, as a leader of the Republican Party, had championed protectionism and high tariffs since the Civil War. In the Senate debate over his antitrust bill he attacked the trusts because they supposedly "subverted the tariff system; they undermined the policy of government to protect . . . American industries by levying duties on imported goods."[7] That is, the price-cutting by the trusts undermined the manufacturing cartel that was created and sustained by the Republicans' high-tariff policies.

The Sherman Act was a political fig leaf designed to deflect attention away from the real source of monopoly power—the tariff—and the true price-fixing conspirators—Congress and protectionist manufacturers. The *New York Times* saw through this charade when it editorialized on October 1, 1890, that the "so-called Anti-Trust law was passed to deceive the people and to clear the way for the enactment of this . . . law relating to the tariff. It was projected in order that the party organs might say to the opponents of tariff extortion and protected combinations, 'Behold! We have attacked the Trusts. The Republican Party is the enemy of all such rings.'"[8]

Economists were almost unanimously opposed to the Sherman Act because they viewed competition as Austrian school economists view it—as a dynamic, rivalrous process of discovery.[9] According to historian Sanford D. Gordon, who surveyed all professional journals in the social sciences and all books written by economists regarding the late-nineteenth-century trusts, "a big majority of the economists conceded that the combination movement was to be expected, that high fixed costs made large scale enterprises economical, that competition under these new circumstances frequently resulted in cutthroat competition, that agreements among producers was a natural consequence, and the stability of prices usually brought more benefit than harm to society. They seemed to reject the idea that competition was declining, or showed no fear of decline."[10]

The Myth That Antitrust "Saved" Capitalism

A popular argument made at the time was that antitrust was necessary to stave off something even worse—the more extreme forms of regulation or outright socialism. Antitrust was adopted, but Americans were subjected to the more extreme forms of regulation—and socialism—anyway. As Milton and Rose Friedman pointed out in *Free to Choose*, by the 1970s the entire Socialist Party Platform

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of 1920 had been adopted in the United States. Socialism, F.A. Hayek pointed out in *The Road to Serfdom*, no longer meant nationalization of industry and central planning, but rather the institutions of the welfare and regulatory state. Antitrust did nothing to stop the spread of socialism in America.

Quite the contrary; the adoption of antitrust helped speed up the adoption of socialism. By weakening the competitive process, it has led to slower productivity growth and diminished prosperity. Government always reacts to slower economic growth, unemployment, and economic crises by adopting even greater economic interventions. The late-nineteenth-century proponents of antitrust had it all backwards. This is why it is so disingenuous, to say the least, of contemporary proponents of antitrust, such as the *Wall Street Journal*'s Murray, to repeat this same discredited argument, urging Bill Gates to "place trust in trustbusters," or else "he may eventually find the Justice Department and Congress considering more-radical remedies."[11]

The Real Robber Barons

John D. Rockefeller, like Bill Gates, achieved his economic success by offering the best products for the lowest prices on the free market. The real "robber barons" of the late nineteenth and the late twentieth centuries are the business people who, having failed to achieve competitive success in the marketplace turned to government and asked it to enact laws and regulations granting them special privileges and harming their competitors. A century ago, such immoral special pleaders included Leland Stanford, who became wealthy by using his political connections to obtain a government-created monopoly franchise in the California railroad industry; Thomas Durant and Grenville Dodge, who pocketed millions in government subsidies to build the Union Pacific railroad; Henry Villard, who "rushed into the wilderness to collect his [government] subsidies" to build the Northern Pacific railroad; and steel industry magnate Charles Schwab, who championed the disastrous 1930 Smoot-Hawley tariff.[12] Their modern-day counterparts would include many of Bill Gates's competitors, such as the chief executive officers of Netscape, Sun Microsystems, Novell, and other companies that have lobbied the federal government to use the antitrust laws to diminish or destroy the competitive efficiency of their most effective rival, Microsoft.

For over 100 years antitrust regulation has allowed politicians to deceitfully pose as "populists" while stifling competition with politically motivated attacks on the most innovative and progressive companies. These attacks have been supported for over a century by socialist intellectuals and journalists who have taught many Americans to hate capitalism, to envy successful people, and to support government policies that undermine or destroy them both. Being the most successful businessman in the world, Bill Gates was an inevitable target of the anti-capitalistic crusaders. It's time we recognized antitrust for the protectionist racket that it is and repealed the antitrust laws. □

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Anything That's Peaceful

Economics: A Branch of Moral Philosophy

by Leonard E. Read

The author of *The Wealth of Nations* (1776) is frequently classed as an eighteenth-century economist. But Adam Smith was primarily a professor of moral philosophy, the discipline which I believe is the appropriate one for the study of human action and such subdivisions of it as may be involved in political economy.

Moral philosophy is the study of right and wrong, good and evil, better and worse. These polarities cannot be translated into quantitative and measurable terms and, for that reason, moral philosophy is sometimes discredited as lacking scientific objectivity. And it is not, in fact, a science in the sense that mathematics, chemistry, and physics are sciences. The effort of many economists to make the study of political economy a natural science draws the subject out of its broader discipline of moral philosophy, which leads in turn to social mischief.

Carl Snyder, long-time statistician of the Federal Reserve Board, exemplifies an economic "scientist." He wrote an impressive book, *Capitalism the Creator*.[1]

I agree with this author that capitalism is, indeed, a creator, providing untold wealth and material benefits to countless millions of people. But, in spite of all the learned views to the contrary, I believe that capitalism, in its significant sense, is more than Snyder and many other statisticians and economists make it out to be—far more. If so, then to teach that capitalism is fully explained in mathematical terms is to settle for something less than it really is. This leaves unexplained and vulnerable the real case for capitalism.

Snyder equates capitalism with "capital savings." He explains what he means in his preface:

> The thesis here presented is simple, and unequivocal; in its general outline, not new. What is new, I would fain believe, is the proof; clear, statistical, and factual evidence. That thesis is that there is one way, and only one way, that any people, in all history, have ever risen from barbarism and poverty to affluence and culture; and that is by that concentrated and highly organized system of production and exchange which we call Capitalistic: one way, and one alone. Further, that it is solely by the accumulation (and concentration) of this Capital, and directly proportional to the amount of this accumulation, that the modern industrial nations have arisen: perhaps the sole way throughout the whole of eight or ten thousand years of economic history.

No argument—none whatsoever—as to the accomplishments of capitalism, or that it has to do with "capital savings." But what is capital?

Leonard E. Read established FEE in 1946 and served as its president until his death in 1983. This article, reprinted from the January 1972 issue of The Freeman, *is the sixth in a monthly series commemorating the 100th anniversary of Mr. Read's birth.*

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The Ideas Behind Capital

The first answer that comes to mind is that capital means the tools of production: brick and mortar in the form of plants, electric and water and other kinds of power, machines of all kinds (including computers and other automated things), ships at sea and trains and trucks and planes—you name it! These things are indeed capital, but is capital in the sense of material wealth sufficient to tell the whole story of capitalism and its creative accomplishments or potentialities?

Merely bear in mind that all of this fantastic gadgetry on which rests a high standard of living has its origin in ideas, inventions, discoveries, insights, intuition, think-of-thats, and such other unmeasurable qualities as the will to improve, the entrepreneurial spirit, intelligent self-interest, honesty, respect for the rights of others, and the like. These are spiritual as distinguished from material or physical assets, and always the former precedes and is responsible for the latter. This is capital in its fundamental, originating sense; this accumulated wisdom of the ages—an overall luminosity—is the basic aspect of "capital savings."

It is possible to become aware of this spiritual capital, but not to measure, let alone to fully understand it—so enormous is its accumulation over the ages. Awareness? Sit in a jet plane and ask what part you had in its making. Very little, if any, even though you might be on the production line at Boeing. At most, you pressed a button that turned on forces about which you know next to nothing. Why, no man even knows how to make the pencil you used to sign a requisition. These "capital savings" put at your disposal an energy perhaps several hundred times your own. This accumulated energy—the workings of human minds over the ages—is capital!

"Truly Scientific"

With this concept of capital in mind, reflect on how unrealistic are the ambitions of the "scientific" economists. Carl Snyder phrases their intentions well in the concluding paragraph of his preface:

> It was inevitable, perhaps, that anything like a 'social science' should be the last to develop. Its bases are so largely *statistical* that it was only with the development of an enormous body of new knowledge that anything resembling a firmly grounded and *truly scientific system* could be established. It is coming; already the most fundamental elements of this knowledge are now available, as the pages to follow will endeavor to set forth. (Italics added)

Snyder is, indeed, statistical. He displays 44 charts. Nearly all of these show the ups and downs—mostly ups—of physical assets in dollar terms. This, in his view is a "truly scientific system." But how scientific can a measurement be if the units cannot be quantified and the measuring rod is as imprecise in value as is the dollar or any other monetary unit?

And what is truly scientific about showing the growth in coal production, for instance, if there be a shift in demand favoring some other fuel? This would be only a pseudo-measurement with no more scientific relevance than a century-old chart showing the dollar growth in buggy whip production.

Professor F.A. Hayek enlightens us: "'All the physical laws of production' which we meet, e.g., in economics, are not physical laws in the sense of the physical sciences but people's beliefs about what they can do. . . . That the objects of economic activity cannot be defined in objective terms but only with reference to a human purpose goes without saying. Neither a 'commodity' or an 'economic good,' nor 'foods' or 'money,' can be defined in physical terms but only in terms of views people hold about things."[2]

National Accounting

Economic growth for a nation cannot be mathematically or statistically measured. Efforts to do so are highly misleading. They lead people to believe that a mere increase in the measured output of goods and services is, in and of itself, economic growth. This fallacy has led to the forced savings programs of centrally administered economic systems—programs which decrease the range of volun-

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When we grasp the point that no man who ever lived has been able to foresee his own future choices, let alone those of others, economic scientism, as it might be called, makes no sense.

tary choice among individuals. This is the heart of the failure of the socialistic policies of the underdeveloped nations of Asia, Africa, and Latin America. As Professor P.T. Bauer has written so eloquently: "I regard the extension of the range of choice, that is, an increase in the range of effective alternatives open to people, as the principal objective and criterion of economic development; and I judge a measure principally by its probable effects on the range of alternatives open to individuals."[3]

Indeed, even an individual's economic growth can no more be measured, exclusively, in terms of historical statistics than can his intellectual, moral, and spiritual growth. These ups and downs cannot be defined in physical terms but only in terms of views people hold about things. These views—highly personal—are in constant flux; you may care nothing tomorrow for that which you highly prize today.

Once we grasp the point that the value of any good or service is whatever others will give in willing exchange, and that the judgments of all parties to all exchanges are constantly and forever changing, it should be plain that even physical assets—money, food, or whatever—do not lend themselves to measurements in the scientific sense.

And when we further reflect on the fundamental nature of "capital savings"—that they emerge out of ideas, inventions, insights, and the like—the idea of scientific measurement becomes patently absurd.

In any event, it is this penchant to make a science of political economy, to reduce capitalistic behavior to charts, statistics, theorems, arbitrary symbols, that leads to such nonsense as the Gross National Product (GNP), "national goals," and "social gains."[4] The more pronounced this trend, the less will the economics of capitalism and the free society be understood—"a dismal science," for certain. Indeed, could the ambitions of the "scientific economists" be realized, dictatorship would be a viable political system. At the dictator's disposal would be all the formulae, all the answers; disregarding personal views and choices, he would simply run his information through computers and thus meet production schedules.

When we grasp the point that no man who ever lived has been able to foresee his own future choices, let alone those of others, economic scientism, as it might be called, makes no sense.

Man's Arrogance

How did we ever get off on this untenable course? Perhaps we can only speculate. A flagrant display: At one point in a recent seminar discussion I repeated, "Only God can make a tree." And then this exclamation by a graduate student, "Up until now!" This, it appears to me, is the reflection of a notion, so prevalent in the eighteenth and nineteenth centuries, that every facet of Creation, even life itself, lies within the powers of man. Merely a matter of time!

To tear human action asunder and then to assign symbols or labels to the pieces, as the scientists properly do with the chemical elements, is no service to economic understanding. This method makes understanding impossible for the simple reason that it presupposes numerous phases of human action that can be mathematically or scientifically distinguished one from the other when such is not the case. Why am I motivated to write this or you to read it? Doubtless, each of us can render a judgment of sorts but it will not be, cannot be, in the language of science.

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Political economy is as easy or, perhaps, as difficult to understand and practice as the Golden Rule or the Ten Commandments. Economics is no more than a study of how scarcity is best overcome, and the first thing we need to realize is that this is accomplished by the continued application of human action to natural resources.

Natural resources are what they are, no more, no less—the ultimate given! The variable is human action.

Political economy, then, resolves itself into the study of what is and what is not intelligent human action. It should attempt to answer such questions as:

Is creative energy more efficiently released among free or coerced men?

Is freedom to choose as much a right of one as another?

Who has the right to the fruits of labor—the producer or nonproducer?

How is value determined—by political authority, cost of production, or by what others will give in willing exchange?

What actions of men should be restrained—creative actions or only destructive actions?

How dependent is overcoming scarcity on honesty, respect of each for the rights of others, the entrepreneurial spirit, intelligent interpretation of self-interest?

Viewed in this manner, political economy is not a natural science like chemistry or physics but, rather, a division of moral philosophy—a study of what is right and what is wrong in overcoming scarcity and maximizing prosperity—the problem to which it addresses itself.

Once we drop the "scientific" jargon and begin to study political economy for what it really is, then its mastery becomes no more difficult than understanding that one should never do to others that which he would not have them do unto him. □

1. Carl Snyder, *Capitalism the Creator* (New York: The Macmillan Company, 1940; Arno Press, 1972).

2. See F.A. Hayek, *The Counter-Revolution of Science* (New York: The Free Press of Glencoe, The Crowell-Collier Publishing Co., 1964), p. 31.

3. P.T. Bauer, *Economic Analysis and Policy in Underdeveloped Countries* (Durham, N.C.: Duke University Press, 1957), p. 113.

4. For more on the GNP fallacy and how economic growth cannot be "factually" reported, see "A Measure of Growth" in my *Deeper Than You Think* (Irvington-on-Hudson, N.Y.: The Foundation for Economic Education, Inc., 1967), pp. 70–84.

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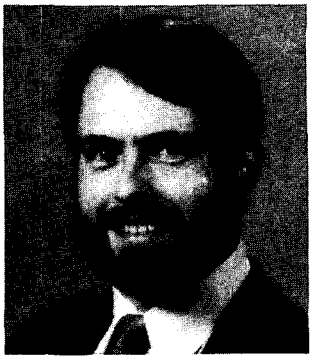

Institutional Immortality, Washington Style

Don't count on your budget surplus before the check clears." That should be this year's motto for taxpayers. Politicians are already debating how to spend the extra money they expect to collect. President Bill Clinton has a $150 billion wish list, and many Republicans are almost as bad. Unfortunately, if last year's budget deal was any example, taxpayers are unlikely to benefit from the predicted budget cornucopia.

The failings of that supposedly historic agreement were many. Federal domestic spending continues to rise even though, adjusted for inflation, it had already risen by a third over the previous decade (nearly four times as fast as family income). Three-fourths of the supposed savings is slated to occur in the year 2001 or beyond, two Congresses away. Moreover, supposedly economy-minded GOP legislators failed to corral any of Washington's most notorious sacred cows.

The Appalachian Regional Commission, a Great Society program devoted to bringing economic growth to Appalachia, still chugs along, no closer to its supposed goal. The Rural Housing Development Service has been providing home loans to farm areas since the Great Depression. The Agriculture Department continues to pay farmers to grow, and not to grow, crops. With the help of federal subsidies, the Tennessee Valley Authority has been providing cheap power to local residents for decades. The Economic Development Administration treats most of the country as depressed and robs taxpayers in one state to underwrite citizens in another. The Agency for International Development takes money from poor people in rich countries and transfers it to rich people in poor countries, subsidizing autocracy and collectivism along the way. The Corporation for National Service pays people to volunteer. All these survive, many with increased funding.

Lack of purpose is no bar to a big bureaucracy and generous budget. Two decades ago the United States suffered an "energy crisis." It was, in fact, a problem of bad policy, not inadequate oil. Richard Nixon limited oil prices as part of his wage and price controls, and preserved the energy restrictions after he ended the rest of the program. The result was increased demand, decreased supply, and, paradoxically, higher imports, since firms with greater domestic reserves had to send checks to those that imported higher-priced foreign petroleum. (As humor columnist Dave Barry says, I'm not making this up—the government forced domestic producers to subsidize oil importers.)

The 1973 OPEC oil embargo caused problems, but far more destructive were the activities of the Carter administration, which created a genuine crisis with a "windfall profits" tax, gasoline-allocation rules, temperature controls in "public" buildings, draconian environmental restrictions, the $88 billion Synthetic Fuels Corporation, and limits on leasing of the Outer Continental Shelf and

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federal lands. So Congress created the Department of Energy, which not only managed all of the dumb old programs that weren't working, but embarked on a host of dumb new ones—efficiency standards for refrigerators and toilets, research for high-cost renewable energy, and the like.

The Department Lives

President Ronald Reagan decontrolled the price of oil in 1981 but did little to kill the department. Now energy supplies are abundant, and the Republican Congress last year . . . voted $15.9 billion for the department, a $100 million increase. Real budget cutters would instead go on a turkey shoot, killing research expenditures that underwrite business, regulatory programs that micromanage consumer choices, and Power Marketing Administrations, which subsidize favored electricity consumers.

At least the Department of Energy is only 20 years old. President Franklin Roosevelt established the Rural Electrification Administration in 1935 to bring power to rural America. Once the agency got going, it, like the Energizer Bunny, never stopped. Virtually every home now has electricity, but the program—recently renamed the Rural Utility Service—continues to provide cheap credit to some one thousand cooperatives across America. Many of the communities being subsidized, like Hilton Head Island and Snowmass, qualify as needy under no one's definition. Except someone living in Washington.

In 1996 the GOP Congress appropriated $2.7 billion for the RUS. Last year the Republicans approved a $300 million increase, including an extra $125 million in loans for distance learning and telemedicine, programs with nothing to do with the agency's original purpose.

Cheaper, at $24 million a year, but no less illustrative, is the Selective Service System. In response to the Soviet invasion of Afghanistan, President Carter imposed draft registration and revived Selective Service. It failed in its purpose of impressing the U.S.S.R.—Soviet leaders could always tell the difference between a list of untrained 18-to-25-year-olds and a sophisticated active-duty force. Moreover, the world in which registration was created has disappeared: the cold war has ended, the Soviet Union has collapsed, and Poland is now a Western-leaning democracy set to join NATO.

Still, registration and Selective Service live on. The President touts the importance of maintaining "the link between the All-Volunteer Force and our society at large," as if filling out a card at the Post Office generates patriotism. Clinton also fusses about sending "the wrong signal to our potential enemies," though the latter are few and pathetic, and would be subdued by the active force before the first conscript emerged from basic training.

Finally, the agency is pushing a "Service to America" initiative. That is, explains Director Gil Coronado, "in our routine communication with all new registrants in America, we encourage them to serve America today," including "community service through the Corporation for National Service." Half of the administration's proposed increase for 1998 was to fund this program, which solicits support for another agency that shouldn't exist. Agency materials speak of "shifting gears" and spokesman Lewis Brodsky admits that Selective Service "can no longer dwell upon its proud past or bet on the threats of tomorrow. The system must be of proven value to America *today and every day*." Thus, the agency is dedicated to simultaneously preventing nuclear war and spreading voluntarism.

When the GOP gained control of Congress in 1994, it targeted some 300 programs. Only a handful have ended. The rest wastefully carry on. There are 342 federal programs devoted to economic development, 163 for job-training, and 131 involving juveniles. Most don't work, but they persist nonetheless. Complains budget analyst Stephen Moore, "as in the Reagan years, Republicans have quickly retreated from the agenda of making government in Washington smaller and smarter." Which is why taxpayers shouldn't expect to ever see their share of the federal budget surplus. □

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THE FREEMAN
IDEAS ON LIBERTY

Natural Society Revisited

by Juliana Geran Pilon

It is heartening that a fashionable new field known as "civil society studies" has recently emerged. It is surely a symptom of concern over whether modern society as we know it is sufficiently civil to foster the growth of Western liberalism. But however distinct the problems of modernity may be, and they surely are, revisiting the original texts of the Enlightenment that first established the field by defining "civil society" seems particularly salutary.

Credit for this renewed interest dating back more than two decades must go to those who most felt its absence. Notes sociologist John A. Hall, "civil society was placed at the forefront of public attention by attempts to establish decency in societies where it had most conspicuously been absent,"[1] particularly by Solidarity in Poland. The term emerged however mainly in a nebulous negative sense, as "the opposite of despotism." The lack of a clear definition is only one reason for the floundering that has characterized efforts to create a genuine civil society in the post-Soviet era.

The nineties have seen a similar resurgence of interest in the idea of civil society in the United States, for reasons that are in some ways similar to what inspired Solidarity: a sense that government is quite powerful and at the same time palpably ill equipped to deal with some of the most pressing problems of our time. The question of how to invigorate a healthy civil society is thus preoccupying pundits and scholars, though not always with felicitous results.

The ambiguity that surrounds the topic of "civil society," as Hall correctly points out, is due to the fact that the concept is "at one and the same time a social value and a set of social institutions."[2] The temptation to address both at once, to judge the social value of a particular type of civil society while defining the set of social institutions that make it up, renders an objective evaluation almost impossible. Hall is correct to attempt to differentiate the two. He offers the following definition: "Civil society is a particular form of society, appreciating social diversity and able to limit the depredations of political power, that was born in Europe; it may, with some luck, skill and imagination, spread to some other regions of the world."[3]

But even this definition does not seem fully capable of shedding normative connotations, for "social diversity" is evidently presented as a value worth "appreciating" while "the depredation of political power" has clearly pejorative connotations. Hall admits to being enthusiastically in favor of civil society, to the point that he "would gladly embrace social tendencies sure to establish civil society even though this would diminish any conception of social agency and human responsibility."[4] Unfortunately, this leaves the reader to wonder just how those "social tendencies" could

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be, how they are to be "fostered," and whether, if indeed they emerge at the expense of "human responsibility," in what way a society where such "tendencies" are exhibited can still be deemed "civil."

The main point, however, is that Hall requires "civil" society to include an "appreciation" of pluralism. This is not true of all definitions. As Adam Seligman notes in his popular book *The Idea of Civil Society*, written immediately after the fall of the Iron Curtain in Hungary and published in 1992, the concept of civil society "has come to mean different things to different people." Yet he observes that the concept "embodies for many an ethical ideal of the social order, one that, if not overcomes, at least harmonizes, the conflicting demands of individual interest and social good."[5] The concept, in other words, seems to imply that society, to qualify as "civil," should seek "the social good" while permitting ("appreciating"?) the need for some "diversity," some notion of "individual interest."

Squaring the Circle

Not wishing to appear libertarian in any way, Seligman is quick to point out that "the problem of liberal-individualist ideology . . . is, how to constitute a sense of community among and between social actors who are conceived of in terms of autonomous individuals."[6] In brief, "civil society" seems to require an internal squaring of what appears to be a vicious circle encompassing "autonomous" individual interests and the (logically and empirically presumed opposite) social good and "a sense of community." How that circle is supposed to be squared while preserving freedom seems to elude Seligman no less than Hall.

It is time therefore to take more seriously the separation between the normative and the descriptive elements of the term, while at the same time resurrecting the elegant discussion of the original idea as presented in the eighteenth century, notably by Adam Ferguson in his still eminently readable *Essay on the History of Civil Society*, published in 1767.[7] It is important to note that the alleged conflict between individual interests and the social good was originally never perceived to be a conflict at all.

Ferguson firmly believed in man's ability—and right—to conduct his affairs as he sees fit. And unlike some of his more misanthropic contemporaries—particularly Edmund Burke, in his brilliant *Vindication of Natural Society*, published in 1756—Ferguson trusts at least some of man's passions, notably "benevolence," which he defines as "no more than a species of self-love."[8] Far from denying that animosity and narrow self-interest are among man's less honorable passions, Ferguson nevertheless finds that man is happiest in the company of others, not only because he is safer in a civil society but also because he finds the presence of others rewarding. Thus "if courage be the gift of society to man, we have reason to consider his union with his species as the noblest part of his fortune."[9]

Interestingly, the term "civil society" as such appears only once in Ferguson's long essay. But that one definition is sufficient to indicate that Ferguson's conception is directly counter to Seligman's contention that "civil society" seeks to reconcile necessarily opposite concepts, namely individual interests and the goals of society. Writes Ferguson: "The happiness of individuals is the great end of civil society: for in what sense can a public enjoy any good, if its members, considered apart, be unhappy?"[10] Society is the sum of its members; a "sum" of their happiness therefore defines the good of all.

In brief, Ferguson's original conception of the civil society defines its end as permitting the exercise of individual freedom, the pursuit of individual goals that are perceived to be good to those who pursue them. At the same time, Ferguson is convinced that men are—or at least can be—naturally benevolent, and believes the feeling of benevolence can be nurtured by underscoring its rational and emotional basis. Not only did Ferguson not see a contradiction between individual and social ends; he saw such a contradiction to be meaningless. Any "public interest" that is opposed to the interests of members of that public cannot possibly be any good.

Ferguson has thus defined the civil society as the "total" of the goals pursued by individ-

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uals seeking their own happiness (and one may add, in full conformity with the spirit of his lengthy essay, at the same time respecting everyone else's right to do the same). What is more, these goals are pursued outside the political realm, or as Burke might have put it, in "Natural Society."

Benevolence as a Form of Self-Love

The normative element that Ferguson clearly adds to this descriptive definition is that a society which makes possible the pursuit of individual goals will also be a desirable, truly "civil" society (in the honorific sense of the term) if its members are benevolent. Benevolence is the great virtue that makes human beings take pleasure in one another's company, desire one another's happiness, and seek to help others in distress. Benevolence is an eminently rational feeling, entirely consistent with self-interest, indeed is a species of self-love.

Accordingly, a civil society where benevolence is nurtured and ubiquitous is eminently desirable and entirely possible. It is absurd to think that man could ever be forced to be either rational or good. To be good, man has to be free. Anything else is meaningless—or at least does not constitute a genuinely civil society.

This brings us to the main difference between the discussion of civil society at the time of the Enlightenment and today. There appears to be strong distrust, not only in formerly communist countries but also in the West, of purely private initiative, of individual freedom, lest it undermine the sense of "community" and "the social good." There seems to be a prevailing fear that people will not behave benevolently unless somehow pressured or even forced to do so. Yet forcing people to pursue "the common good" rather than respecting each person's right to pursue his own happiness as he sees fit (while respecting everyone else's right to do the same) can only result in a society that may seem civil but is only dubiously free.

Ferguson's definition of "civil society" as the "total" of individual goals pursued in an atmosphere of mutual respect necessarily implies "an appreciation of social diversity." It repudiates however the supposed tension between individual interests and the social good. That tension should not exist in a society that nurtures benevolence in a manner that is consistent with the principle of human responsibility. And in any event, a society that dispenses with responsibility cannot be called "civil" in either a descriptive or normative sense of the term.

Civil society is certainly not guaranteed by freedom. Freedom requires stable institutions and the rule of law. Without freedom, however, society can be called "civil" only at the expense of both semantic honesty and the nature of human action. Community and benevolence should not be seen as antithetical to the pursuit of individual interests; it was not perceived that way by the philosophers who first conceptualized "civil society."

Adam Ferguson defended the proposition that the interests of the individual and those of society are "easily reconciled" with the following observation: "That is the most happy state, which is most beloved by its subjects; and they are the most happy men, whose hearts are engaged to a community, in which they find every object of generosity and zeal, and a scope to the exercise of every talent, and of every virtuous disposition."[11] That community will not happen by force. It should not have taken the terrible reality of communism to prove that simple fact. □

1. John A. Hall, ed., *Civil Society: Theory, History, Comparison* (Cambridge, England: Polity Press, 1995), p. 2
2. Ibid., p. 3.
3. Ibid., p. 25.
4. Ibid., p. 3.
5. Adam Seligman, *The Idea of Civil Society* (New York: The Free Press, 1992), p. x.
6. Ibid., p. 204.
7. Adam Ferguson, *An Essay on the History of Civil Society* (New Brunswick, N.J.: Transaction Publishers, 1991).
8. Ibid., p. 14. See Edmund Burke, *A Vindication of Natural Society* (Indianapolis: Liberty Classics, 1982).
9. Ferguson, p. 19.
10. Ibid., p. 58.
11. Ibid.

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THE FREEMAN
IDEAS ON LIBERTY

The Origin of Religious Tolerance

by Wendy McElroy

In 1733 the philosopher credited with ushering in the French Enlightenment, François Marie Arouet de Voltaire, published *Letters Concerning the English Nation*. It was a pivotal work. Although written in French, the 24 letters were first issued from London in an English translation; the material was considered too politically dangerous for the author or any French printer to have the work to appear in France.[1]

Voltaire was no stranger to such controversy. Some years before, after being beaten up by the hirelings of an aristocrat whom he had offended, Voltaire had been thrown into the Bastille (for the second time). He was released after pledging to stay at least 50 leagues away from Paris. Voltaire chose to go as far as England, where he stayed for roughly two-and-a-half years. The result of the sojourn was the *Letters* on English religion and politics, written as though to explain English society to a friend back in France. They finally appeared in France in 1734 as *Lettres philosophiques*, or *Philosophical Letters*.

Letter five, "On the Church of England," began with the observation, "This is the country of sects. An Englishman, as a freeman, goes to Heaven by whatever road he pleases." The statement had profound implications for any citizen of France—a nation that had almost destroyed itself in order to establish Catholicism as the only practiced religion.

In the next paragraph, Voltaire pursued a theme that contributed heavily to the danger of publishing his work in France: he examined the intellectual and institutional foundation of England's religious tolerance. First, he rejected a political explanation. Referring to the established Church of England, he acknowledged that politics strongly favored prejudice rather than tolerance. He wrote, "No one can hold office in England or in Ireland unless he is a faithful Anglican."[2] Such political exclusion hardly promoted religious good will.

Nor did the religious preaching of the dominant church lead the nation toward toleration. According to Voltaire, the Anglican clergy worked "up in their flocks as much holy zeal against nonconformists as possible." Yet in recent decades, the "fury of the sects . . . went no further than sometimes breaking the windows of heretical chapels."

What, then, accounted for the extreme religious toleration in the streets of London as compared to those of Paris?

The Peace of Commerce

In letter six, "On the Presbyterians," Voltaire ascribed the "peace" in which "they [Englishmen] lived happily together" to a mechanism that was a pure expression of the free market—the London Stock Exchange. In the most famous passage from *Philosophical Letters*, Voltaire observed, "Go into the

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Voltaire

Exchange in London, that place more venerable than many a court, and you will see representatives of all the nations assembled there for the profit of mankind. There the Jew, the Mahometan, and the Christian deal with one another as if they were of the same religion, and reserve the name of infidel for those who go bankrupt."

Legally and historically, England was no bastion of religious toleration: laws against nonconformists and atheists were still in force. Yet in England, and not in France, there was an air of toleration on the street that existed quite apart from the law. Even though both countries had aristocracies, England was not burdened with the unyielding class structure that crippled social and economic mobility in France. As Voltaire wrote in letter nine, "On the Government": "You hear no talk in this country [England] of high, middle, and low justice, nor of the right of hunting over the property of a citizen who himself has not the liberty of firing a shot in his own field."

A key to the difference between England and France lay in the English system of commerce and in the comparatively high regard in which the English held their merchants. (This is not meant to slight the substantial differences between the English and French governments—especially the constitutional ones—upon which Voltaire dwelled.) In France, aristocrats and the other elites of society regarded those in commerce with unalloyed contempt. In letter 10, "On Commerce," Voltaire pointedly commented on the French attitude: "The merchant himself so often hears his profession spoken of disdainfully that he is fool enough to blush." Yet in England, the "merchant justly proud" compares himself "not without some reason, to a Roman citizen." Indeed, the younger sons of nobility often entered commerce or took up a profession. This difference in attitude was a large factor in explaining the extraordinary rise of the English middle class, their wealth deriving from trade. Indeed, the French often derided England as a nation of shopkeepers. Voltaire thought this was a compliment, observing that if the English were able to sell themselves, it proved that they were worth something.

Commerce, or shopkeeping, established an arena within which people dealt with each other solely for economic benefit and, so, ignored extraneous factors such as the other party's religious practices. On the floor of the London Stock Exchange, religious differences disappeared into background noise as people scrambled to make a profit from one another. The economic self-interest of the Christian and the Jew outweighed the prejudice that might otherwise sour personal relations between them. They intersected and cooperated on a point of common interest: "the Presbyterian trusts the Anabaptist, and the Church of England man accepts the promise of the Quaker," Voltaire wrote in "On the Presbyterians."

Voltaire Versus Marx

Ironically, Voltaire singled out for praise precisely the same aspect of commerce—the London Stock Exchange—that Karl Marx later condemned. Both viewed the marketplace as impersonal or, in more negative Marxist terms, dehumanizing. For Marx, people in the marketplace ceased to be individuals expressing their humanity and became interchangeable units who bought and sold. To Voltaire, the impersonal nature of trade was a good thing. It allowed people to disregard the divisive human factors that had historically disrupted society, such as differences

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"If there were only one religion in England, there would be danger of tyranny; if there were two, they would cut each other's throats; but there are thirty, and they live happily together in peace."

—VOLTAIRE

"On the Presbyterians"

of religion and class. The very fact that a Christian who wished to profit from a Jew, and vice versa, had to disregard the personal characteristics of the other party and deal with him civilly was what recommended the London Stock Exchange to Voltaire.

In this, Voltaire's voice is reminiscent of Adam Smith in his most popular work, *The Wealth of Nations*. Smith outlined how everyone in a civilized market society is dependent on the cooperation of multitudes even though his friends may number no more than a dozen or so. A marketplace requires the participation of throngs of people, most of whom one never directly encounters. It would be folly for any man to expect multitudes of strangers to benefit him out of sheer benevolence or because they like him. The cooperation of the butcher or the brewer, said Smith, was ensured by their simple self-interest. Thus, those who entered the marketplace did not need the approval or favor of those with whom they dealt. They needed only to pay their bills.

The toleration created by the London Stock Exchange extended far beyond its doors. After conducting business with each other, the Christian and the Jew went their separate ways. As Voltaire phrased it, "On leaving these peaceable and free assemblies, some go to the synagogue, others in search of a drink. . . ." In the end, "all are satisfied."

The *Philosophical Letters*—Voltaire's tribute to the English middle class, their commerce, and their society—created an enormous impact on the European intellectual scene. Calling the work "a declaration of war and a map of campaign," Will and Ariel Durant commented: "Rousseau said of these letters that they played a large part in the awakening of his mind; there must have been thousands of young Frenchmen who owed the book a similar debt. Lafayette said it made him a republican at the age of nine. [Heinrich] Heine thought 'it was not necessary for the censor to condemn this book; it would have been read without that.' "[3]

The French Reaction

Nevertheless, French censors seemed eager to condemn it. The printer was imprisoned in the Bastille. A *lettre de cachet* for the elusive Voltaire's immediate arrest was issued. By a legislative order, all known copies of the work were confiscated and burned in front of the Palais de Justice. Through the intercession of powerful friends, the *lettre de cachet* was withdrawn, again on the promise that he remain safely outside the limits of Paris. In this manner did the French church and state respond to Voltaire's salute to toleration.

But the themes of the *Philosophical Letters* resounded deeply within the consciousness of Europe for many decades to come. One of its themes was that freedom—especially freedom of commerce—was the true wellspring of religious toleration and of a peaceful civil society. The insight was nothing short of revolutionary because it reversed the accepted argument and policies on how to create a harmonious society. Traditionally, France (along with most other European nations) attempted to enforce a homogeneous system of values on its people in the belief that common values were necessary to ensure peace and harmony, the social glue that held

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together the social fabric. This was thought to be particularly true of religious values.

This was not a moral argument, but a practical one: society would collapse into open violence without the cohesion provided by common values. Thus, those in authority needed to centrally plan and rigorously enforce the values that should be taught to and should be practiced by the masses. After all, if people were allowed to choose their own religious values, if values became a commodity open to competition, then civil chaos and conflict would inevitably ensue.

Voltaire argued that precisely the opposite was true. The process of imposing homogeneous values led only to conflict and religious wars. The result was a society intellectually stagnant and morally corrupt, because doubt or dissent was suppressed. It was diversity and freedom that created a thriving and peaceful society. Voltaire ended his most-quoted letter, "On the Presbyterians," by observing: "If there were only one religion in England, there would be danger of tyranny; if there were two, they would cut each other's throats; but there are thirty, and they live happily together in peace."

Perhaps one reason that Voltaire's *Philosophical Letters* created such a backlash from the French leviathan was that the book's logic, if carried beyond religion, would strike at any government attempt to impose common values or practices on the people. Indeed, Voltaire's argument against homogeneity continues to have deep implications for the centralized policies of all governments. Those citizens who reject imposed homogeneity in religion might well be prompted to question the wisdom of many other government institutions, including public schools, which are often justified by the declared need for common values. The freedom of individuals to decide matters of value for themselves could easily prompt them to demand the right to live according to those values and to teach them to their children. Thus could the system of centralized control unravel. □

1. The number of letters included varies slightly from edition to edition. The one used as a source for this article, *Philosophical Letters,* trans. Ernest Dilworth (New York: Macmillan Publishing Company, 1961), contains 25.

2. Among the political barriers for non-Anglicans was the Test Act of 1673, which required the holders of public office to receive the sacrament in the Church of England.

3. Will and Ariel Durant in *The Story of Civilization: Part IX, The Age of Voltaire* (New York: Simon and Schuster, 1965), p. 370.

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THE FREEMAN
IDEAS ON LIBERTY

A Peaceful Ferment in Somalia

by Spencer Heath MacCallum

A social experiment with far-reaching implications for human freedom is shaping up in Somalia. I had known that something was afoot but learned the details only last summer on meeting a Somali tribeswoman traveling in the United States with her European husband. She was an elegant, educated lady who would have been at home in any of the great cities of the world. When her husband introduced me as an anthropologist with classical liberal leanings, conversation turned toward her tribe, an independent, nomadic people who control and move over a large area on both sides of the Somalo-Ethiopian border. Hers is one of a constellation of tribes sharing similar language, culture, and customary law that for countless centuries lived together in relative harmony in that easternmost jut of the continent known as the Horn of Africa. The Somali nation by tradition, she said, is a stateless society; they have never accepted the authority of any central government, their own or any other.

Then she asked a question that took me by surprise: "Do you think it possible that my people could come into full participation in the modern world—culturally, scientifically, economically—without becoming a part of any state?" I told her I'd thought about that possibility with respect to tribal peoples for many years, but had never expected that anyone would ask the question. I said I thought it was theoretically possible, but that it would take extraordinary patience, careful planning, great flexibility. The way was untraveled.

As we talked, she explained an approach that Somalis from several tribes had discussed. It involves capitalizing on their statelessness by opening areas within their tribal lands for development, inviting businessmen and professionals the world over to come to take advantage of the absence of a central government or other coercive authority. In this way Somalia's statelessness might prove to be a uniquely valuable asset in the modern world.

Specifically, they were considering offering suitable tracts within their tribal lands on long-term lease for private development. Such development would take the pattern of large multiple-tenant income properties—"estates," as the British would call them—where the land would be leased but the improvements would be privately owned. An attractive site under consideration by my friend's tribe was a sparsely populated upland valley, which because of its elevation enjoyed a temperate climate yet also had access to the sea.

An industrious population, the tribespeople reasoned, attracted from all quarters of the globe by the promise of unprecedented personal and business freedom, could make such areas productive enterprise zones. Some of the more successful zones might eventually become bustling cities not unlike the free

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cities of medieval Europe that began the modern age. Such an arrangement would yield the tribes an income; their members would enjoy a dignified status as the ultimate landlords; and they would have available to them in their own backyard, as it were, an abundance and variety of educational, training, and work opportunities. It would be their steppingstone to full entry into the modern world. This was the dream that my friends shared with me on a summer afternoon.

The Chaos That Isn't

Other Americans they had mentioned this to were horrified. All had a similar picture in mind. From media reports, they knew—or thought they knew—contemporary Somalia to be in unrelenting chaos, ravaged by warfare, starvation, and disease, the battleground of rival warlords such that people could neither put in their crops nor harvest them if they did. What else could one expect of a country that had been without a central government for seven years? But my friends said this picture is sadly exaggerated. While there is a modicum of fighting and disorder in some areas, most notably in the south, the overall picture is far different. Many Somalis, they said, are finding that the absence of a central government has its advantages.

Having been influenced by the same media, I was skeptical. But the possibility that my friends might be right was so intriguing that over the next few months I found myself looking for corroboration. It came from many places. First, a *Los Angeles Times* article, titled "A Somali Alternative to Chaos," described the prosperity of the seaport of Bosaasso in northeastern Somalia. Its opening words were, "Near the tip of the Horn of Africa, a port city is booming, helped by a lack of clan warfare and the absence of a central government."[1]

Next was a signed newspaper editorial in Addis Ababa, Ethiopia, titled, "Does Somalia Really Need a Government?" There could be no doubt that the author, Mohamed Mohamed Sheikh, was a qualified observer. Born in Somalia, south of Bosaasso, he had worked in Mogadishu as a radio reporter, then in the information services of various ministries, and finally as a consultant with UNESCO. He wrote that "donor countries and international financial institutions . . . are uneasy with the Somali experience which they perceive as dangerously contagious. In fact, the Somali experience is rather confusing for the ordinary minds. Who could imagine that Somalia exports today five times more than in 1989, the last year of which official estimates are available."

He went on to state that the economy of Somalia "functions as a perfect model of 'laissez-faire' as conceived by Adam Smith. Government spending is reduced to zero and inflation is very low. The Somali shilling is freely convertible in the market and exchange rates are more stable than in most African countries." He also said that "telecommunications and air transport have made tremendous development during the last seven years. . . . Indeed, Somalia has no customs authorities and all goods are imported duty free. New schools and clinics are opening every day, offering their services to those who can afford to pay."[2]

In the absence of statistics, I wondered how Mohamed Mohamed obtained his information that Somali exports had increased fivefold? In correspondence with me, he explained how he had carried out field research, what assumptions he had made, and how he defended his conclusion. The approximation sounded reasonable, however rough.

More evidence was a lengthy report in the APC-EC *Courier*, published by the Commission of the European Communities, Brussels.[3] The report notes that "The outside world's picture of Somalia has been distorted by the natural tendency of the foreign media to focus on bad news." It goes on to say that "In the absence of a central government, Somalia has fractured into dozens of different fiefdoms with all manner of competing and overlapping authorities." Yet, states the report, "Peace reigns in most of the country. Regional and local governments have been able to resume working in many areas, albeit on a minimal basis."

The report continues that the markets in towns and cities had a large variety of imports and that local entrepreneurs were furnishing consumer products and jobs. "They now provide many services normally associated with government," it says. "The lack of state struc-

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Foolish Inconsistencies

When a domestic steel producer solemnly croons for the television cameras about how high tariffs on imported steel are good for the American economy, you can be sure that he is not really interested in the well-being of his fellow citizens. He is undoubtedly a swindler motivated by no ideal more elevated than fattening his own wallet at the expense of American consumers. The same is true of the great majority of interest groups whose lobbyists infest Washington and other seats of government power.

It's a mistake, however, to suppose that *all* champions of intrusive government are out for gains at the expense of others. Many proponents of high taxes and intrusive government sincerely believe that the state can outperform the market.

The sincerity of such beliefs, however, does not render them correct. Indeed, even the most sincere statist is typically so confused that his ideas are a muddle of foolish inconsistencies.

Consider that statists are firmly convinced that capitalism is bad because capitalists are concerned exclusively with squeezing every drop of profit out of their businesses. And yet, many statists are no less firmly convinced that capitalism promotes racial and sex discrimination.

Both beliefs can't be true. If capitalists care *only* about the bottom line, they will energetically pursue profitable deals with anyone regardless of skin color or sex. A capitalist focused only on maximizing profits will not refuse to hire a black woman if this black woman promises to add greater net value to the firm than does a white man competing for the same job. To be single mindedly focused on profit is to be unconcerned about irrelevant matters such as employees' or customers' skin color or sex. In contrast, a capitalist intent on satisfying his own racial or sexual bigotry when hiring employees or choosing customers will not focus exclusively on the bottom line.

Statists also believe that large corporations are simultaneously obsessed with profits *and* indifferent to relatively small expenses. I attended a conference recently at which a participant remarked that a $1 million per day fine doesn't bother Microsoft "because Microsoft is worth billions." Perhaps. But if the company is indeed indifferent to being fined $1 million per day, then it is not (contrary to accusations) dogged about maximizing its profits. Microsoft and other corporations will not be cavalier about even small unnecessary expenses if these corporations in fact are consumed with a passion for making their bottom lines as large as possible.

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Among my favorite statist inconsistencies is their insistence, in one breath, that income inequality is an evil of the first rank, along with the accusation in the next breath, that free-market advocates have an unsavory concern with material matters. Enemies of the market are forever applauding themselves for recognizing that non-material pursuits are far more ennobling and satisfying than the pursuit of financial gain.

Well, if non-material pursuits are deeper and more rewarding than are material pursuits, then income inequality should rank very low on statists' list of capitalist outrages. The minimalist poet earns far less money than does the CEO of Coca-Cola, but the poet presumably enjoys far greater spiritual and mental rewards than does the corporate chieftain. Rather than taxing the CEO more heavily than the poet, perhaps government should offer the CEO a *lower* tax rate to help compensate him for his meager spiritual rewards.

Statists are also inconsistent in their assessments of self-interested actions. Corporations are scolded for seeking profits for their shareholders, while labor unions are glorified for seeking higher wages for their workers. There are, of course, differences between the self-interested actions of private corporations and those of labor unions. Corporations unaided by government privilege profit only by making those with whom they deal better off. Modern labor unions, in contrast, derive most of their effectiveness from government privileges and achieve their gains only by making those with whom they deal—and even many with whom they do not deal!—worse off.

Another statist inconsistency is the confused attitude toward change. Statists today condemn the market because it brings change. Once-thriving industries are rendered obsolete by newer products and sources of supply. Towns once built around a particular industry are depopulated by the demise of that industry. Dejected workers, pink slips in hand, trudge haplessly across the television screen. Abandoned factories, windows broken and weeds overrunning their parking lots, appear in *faux*-poignant newspaper photos. The message is clear that market forces unfeelingly unleash immense changes that upset familiar and cherished ways of life.

The market is indeed a force for change, but always change that results in far more improvement than harm. Anyone who doubts that the market is a continual source of improvements for humankind need only reflect on what life in America was like, say, 50 years ago. Polio still raged, only the wealthy elite could afford air travel, all but the very rich sweated through the summer heat without air conditioning, and even top-of-the-line automobiles broke down with appalling frequency. Advances spawned by entrepreneurs and made widely available by the free market solved these and countless other problems that plagued Americans in 1948.

It's true that workers who manufactured iron lungs for polio victims suffered job losses when Dr. Jonas Salk rendered their services unnecessary. But should we condemn the market for this change? Or should we applaud the market for making possible Salk's cure? The answer is obvious—and the same answer holds for all changes, big and small, promoted by free markets.

Yet it is these improvements that statists condemn—while going on in speech after speech about the nobleness of efforts to "change the world."

They can't have it both ways. If change is bad, then it's bad whether it's achieved by government or by markets. If some change is acceptable, then statists must make the case that change sponsored by government is superior to change sponsored by markets. But such a case is never made. Statists are content to condemn market-directed change and to praise all change that results in greater politicization of our lives.

If inconsistency of thought is a symptom of bad ideas, then the "ideas" sported by statists are surely about as bad as ideas get.

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DANIEL B. KLEIN received his bachelor's degree in economics at George Mason University (1983) and his doctoral degree at New York University (1989). He is now associate professor of economics at Santa Clara University. He has worked and published with the Cato Institute, the Reason Foundation, the Independent Institute, the Institute of Economic Affairs, the Brookings Institution, and the Foundation for Economic Education.

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tures means no bureaucratic interference. Somalis seem particularly well adapted to operating in such an environment. . . . The clan tradition makes any form of central government difficult here. . . . Somalis consider themselves born free. To them, the State equals registration, regulation and restriction."

All these reports, and more, lent credence to my friends' statement that when the Somalis dismantled their state in 1991, tribal governments had quickly filled the vacuum. That had come as a surprise, they said, to those who remembered the determined efforts of the state to eliminate Somalia's traditional judges and police from the political scene. But tribal government remained the government of choice for Somalis. According to my friends, this indigenous government, composed of part-time police and law courts, had been effective during the past seven years in keeping the peace in the rural areas. They said that many observers thoughtlessly describe this situation as anarchy whereas, in reality, it is government based on natural law.

Unraveling the Somali Political Equation

Before the colonial era, the homeland of the Somali nation was the whole of the Horn of Africa, bounded on the north and east by the Indian Ocean, on the south by the Tana River in what is now Kenya, and on the west by the Ethiopian and Galla highlands. It was fragmented into five parts by the colonial powers—France, England, Italy, and Ethiopia. In 1960, the British withdrew from the north and the Italians from the south, leaving in their place one government over the former two colonies. There resulted a v-shaped country, the Republic of Somalia—a 1,600-mile belt of coastline around both sides of the Horn with an average depth of some 200 miles.

The French subsequently withdrew from the extreme northwest coast, leaving the Republic of Djibouti. A fourth part of the original Somali nation is now controlled by Kenya. The fifth part lies inland, comprising the heartland of the Horn. It is wholly within Ethiopia and nominally independent—hence unrestricted movement is permitted between Ethiopia and Somalia.

Soon after the British and Italian withdrawal, the Somalis realized that independence had not made them free. The foreign oppressors had left, but their tool of oppression, the state, remained intact. Three decades later, therefore, with the intention of restoring the pre-colonial indigenous political tradition, the leading tribes within the republic joined forces and deliberately dismantled the central government. The United Nations attempted militarily to reinstate it but was defeated, and Somalis themselves made several splinter attempts at state formation, notably in Mogadishu and Hargeisa. Such attempts accounted for most of the turmoil in the years following the dissolution of the central government in 1991.

The basic problem confronting the Somalis is that voting democracy cannot work in a tribal or clan system, where any coercive political apparatus with power to tax and confer patronage is seen as a prize to be controlled for the benefit of one's kindred. The presence or even the prospect, therefore, of a state apparatus keeps the country in continual agitation.

That explains the Somali "warlords." These are warriors who gain their support within their tribes by holding out the promise that they will re-establish the state and control it in order to grant privileges to their kinsmen and prevent others from doing the same to them. In dismantling their state in 1991, the Somalis did not realize that the mere possibility of a future state would be enough, in the short term at least, to prevent peace from returning to their country. If the tribes could convincingly declare that their territory would remain forever stateless, no one would listen to these warriors and they would have no option but to place themselves again under the discipline of tribal customary law. The Somali nation would have neutralized its warlords.

Unfortunately, there has been no practical possibility of that happening. The mere likelihood of a central government has been like the golden apple of Eris, Greek goddess of discord. Eris rolled a golden apple into the hall on Mount Olympus where all the gods were partying without (for good reason) having invited her. Inscribed "For the fairest," the golden apple quickly accomplished its intended purpose of setting the gods to fighting.

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This was the Somalian stand-off for seven years, with the country gradually stabilizing as the prospect of a new Somali state receded. Were there such a category, Somalia would now qualify for the Guinness record for the country with the longest absence of government. Meanwhile, the world's "family of nations" has become increasingly uncomfortable that any place on the globe should be outside the jurisdiction of a state, especially for a significant length of time and with indications that its inhabitants might not only survive, but prosper.

Could anything be more unsettling to those having a stake in perpetuating widespread belief in the necessity of the state? Moreover, the donor governments and international financial organizations mentioned by Mohamed Mohamed Sheikh cannot very well regulate a national economy in the absence of a central government into which to channel funds. Since the failure, therefore, of the first international attempt to restore the Somali state, pressure has been building for a second.

Plans took shape for a "Somali peace conference" in November 1997. Participating would be the United Nations, European Union, Arab League, Italy and Ethiopia, with U.S. funding. Their reported agenda: to bring an end to chaos and restore peace in Somalia by instituting a central government. The European Union engaged a London university professor to draft a constitution and, as incentive for the Somalis, promised a substantial financial aid package for the new government.

Twenty-six Somali political groups, most led by military figures, met in Cairo. The resulting "Cairo Accord" declared a provisional government in which one of Somalia's larger tribes, the Hawiye, would assume the key executive positions and control more than 50 percent of the votes in the parliament. Despite its strong endorsement by the UN, the European Union, and the Arab League, the accord was soon forgotten. Significantly, almost none of the negotiations had dealt with the constitutional questions of what powers the new state should have or how they should be limited; the only issue was how control would be shared among the mostly military figures present.

The "American Text"

Then a small group of Somalis, including my friends, received from private sources in the United States a proposal for a Somali constitution drafted by anthropologist and businessman James C. Bennett of Baltimore. It was offered as an alternative to the constitution drafted in London, and the two were soon dubbed the "English text" and the "American text." The latter provided for a government of such exceedingly limited functions that it could not become a bone of contention simply because it held out no prospect of power and patronage. It would provide the structure of a central government as required by the international community while scrupulously preserving the autonomy of the tribes. The basic principles of the American text include:[4]

Sovereignty. Sovereignty resides in individual Somali citizens, over whom the Somali Federation shall exert no powers. The Federation's main purpose will be to conduct a foreign policy, to enable foreigners to deal with the Somali nation as a whole, and to make the Somalis credible in the eyes and minds of foreign governments and individuals. It shall not regulate relations between Somalis, between Somali communities, nor between Somali regions. The *Xeer* (customary law, pronounced "hair") will govern that.

Customary Law. The Somali nation has always been based on the *Xeer*, even during the period of colonization (for disputes involving only Somalis and not colonials) and after independence. The unity and peace of the Somalis, as well as their mutual understanding, are based on the *Xeer*. The *Xeer* stands at the center of the Somali identity; without it there could not be a Somali nation.

Foreign Policy. The Somali Federation will appoint federal ambassadors abroad, but every tribe will be entitled to appoint its own consuls, who shall enjoy federal status. Debts to foreigners incurred by the Somali state prior to its collapse in January 1991 will be settled by a corporation to be established by the new Federation.

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Peace and Development. To preserve the peace and facilitate the development of the nation, the Somali Federation shall have no police, no military, no taxation, no courts of law, and no majority rule.

If the American text should become the basis for a national organization of the Somalis, it would open the way for the tribes to develop enterprise zones or free cities as a bridge to full participation in the modern world. But success would depend on a stable social environment within Somalia that offered effective protection of private property and freedom of contract. In a situation of autonomous tribes and no strong central government, how would this be assured?

Kritarchy

I began by saying that a social experiment with far-reaching implications is shaping up in Somalia. That experiment consists in the Somalis seeking an alternative to legislative law by looking to their existing customary tribal law, the *Xeer*, and its further development to serve all of the needs of an emerging urban society. The *Xeer* promises to become one of the great bodies of customary law, like Anglo-American common law or Jewish traditional law (*Halacha*). These legal codes are flexible, responsive, and can be maintained without a large central state or legislative apparatus.

A small amount of private funding has just been committed to begin codifying the *Xeer*. While the *Xeerada* (plural) appear to vary from tribe to tribe, it is only because each contains mythology particular to its tribe. In essence, the *Xeerada* are alike in protecting freedom of movement, free trade, and other individual freedoms, and forbidding the contrary—including taxation and legislation.

The Somali nation did not start with the tribes having a common language but by their common observance of the *Xeer*. Hence the law is called both father and child of the Somali nation.

A society organized strictly in accordance with the *Xeer* is technically a "kritarchy," as opposed to a democracy, theocracy, monarchy, oligarchy, or other form of political government. The term, a little-used nineteenth-century word compounded from the Greek, literally means "rule by judges." Many stateless societies have been kritarchies, including the well-known example of the Old Testament Jews during the time of the Judges. The proposed free enclaves also would be kritarchies, since they would be founded solely on the principles of successful modern commerce and the traditional *Xeer*.

One principle of the *Xeer*, like that of the customary law of many kritarchies, is that the clan or other kinship group in effect insures its members, paying compensation in the event any of its members injures someone of another group. This is how the various Somali tribes in the absence of a central state managed to live for untold centuries in relative harmony. It is a principle ideally suited for adaptation to an urban society, where that function can be performed by commercial insurance. The only requirement, in fact, of visitors to Somalia under the proposed constitution would be that they have adequate insurance against any liability that might incur under the *Xeer*.

I wish my Somali friends well. Such a radical experiment to find better ways of protecting private property and freedom of exchange, the underpinnings of all other freedom, is long overdue in the world. It was in 1776 that the last great experiment of this kind was made. Whether or not it succeeds today as envisioned by my friends, this intellectual ferment in Somalia augurs a better future for us all. □

1. Ann M. Simmons, "A Somali Alternative to Chaos," *Los Angeles Times*, July 9, 1997.

2. Mohamed Mohamed Sheikh, "Does Somalia Really Need a Government?" Signed editorial in *The Sun*, Addis Ababa, Ethiopia, August 28, 1997. It is not quite true that imports are duty free, as stated here, but they are virtually so, since port officials need only levy what little is required locally to operate the port.

3. Simon Horner, "Somalia: A Country Report," APC-EC Courier (Commission of the European Communities in Brussels) No. 162, pages 46–66.

4. I have slightly edited and abbreviated these principles from a draft received December 22, 1997, from my Somali friends, to whom I am indebted as the chief source of information used in this article. Until such time as they no longer wish to remain anonymous, inquiries about these libertarian developments in Somalia can be directed to me at SM@Look.net or by regular mail at P.O. Box 180, Tonopah, NV 89049.

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The Idiocy of Autocracy

In any dictatorship, the biggest fool is the dictator.

It takes a prodigious amount of self-deception to believe you are running a country. I was reminded of that as I heard about Fidel Castro's preparations for the Pope's visit to Cuba last winter. In an interview on Cuban television, Castro said he didn't think the visit would lead to the end of socialism in Cuba. (John Paul II, of course, is widely credited with contributing to the peaceful toppling of the Soviet-backed regime in his native Poland.) Here is where the Cuban ruler reveals the depths of his self-deception.

There is no socialism in Cuba.

Consider this headline in the *Washington Post* just before the visit: "Cubans Scurry To Capitalize On Papal Visit, Cost of Hotels, Services Soars for Foreign Influx." Translation: the Cuban people are entrepreneurs behaving as though they live in a capitalist country. Almost 40 years of "socialism" have failed to propagandize or breed capitalism out of them. Could capitalism be the political economy of human nature? It would seem so.

But is there really no socialism, or communism, in Cuba? We have been told for decades that Castro is a Marxist. He claims to be in the vanguard of the Marxist revolution. As Marx wrote of it, socialism was not only to include state ownership of the means of production, but also the abolition of markets, money, and exchange. In Cuba the state owns the major industries and the land; nevertheless, there are markets, money, and exchange. Castro may think he and his experts plan the economy, but that is the biggest self-deception of all.

Every day the Cuban people make countless decisions, transactions, and calculations about which the dictator and his bureaucrats will never know anything. Thanks to the black and gray markets, Cubans most of the time buy and sell and produce, within constraints, according to their own lights. The "planners" issue decrees, but they know they will often be ignored. Even if they are obeyed, the planners can't know what the rippling unintended consequences will be. Often they are opposite of what was expected. Human action is unpredictable that way.

Ask yourself: how can the small group of bureaucrats constituting the government of Cuba possibly direct the actions of over ten million people, each with his own preferences and aspirations? It would take as many bureaucrats as citizens to attempt to pull that off. But even that wouldn't help, because the bureaucrats themselves are already too busy wheeling and dealing. The government calls that "corruption." But for such corruption the people would have all starved long ago.

The plan is a sham. If Castro has any sense, he knows it.

In a path-breaking demolition of socialist theory almost 80 years ago, Ludwig von Mises called socialism "impossible." He meant that literally. He was ridiculed for making what seemed a patently absurd statement. As years passed, people, pointing to the Soviet Union, asked how socialism could be impossible.

Sheldon Richman is editor of The Freeman.

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The critics missed Mises's point. The great liberal and Austrian economist had said that an economy of any complexity could not adequately satisfy consumers in the absence of money, markets for capital goods, and private property because people would have no way to make the calculations necessary to comparing and choosing among alternative uses of resources. Prices permit disparate things—a supply of steel, a parcel of land, a machine, a quantity of labor services—to be stated in terms of a common denominator, the monetary unit. They can then be subjected to calculation. The balance sheet can be filled out. Entrepreneurs can compare the price of the factors of production with the price of final consumer goods and determine if they will have a profit or loss at the end of the day. That information reveals whether resources are being used as consumers wish.

Responding to Mises, so-called "market socialists" said prices could be simulated through bureaucratic trial and error or by solving a series of equations. Startlingly, even some who grasped the virtues of capitalism agreed: the renowned Harvard University economist Joseph Schumpeter declared the socialists the winners in the famous "calculation debate" launched by Mises and carried on by F.A. Hayek. Directly repudiating Mises by name, Schumpeter wrote in *Capitalism, Socialism, and Democracy* (Harper & Brothers, 1942, p. 172), "There is nothing wrong with the pure logic of socialism."

Hayek countered the "market socialists" by pointing out that real prices cannot be created by simultaneous equations or by bureaucrats playing at markets. Those prices would be empty, in contrast to market prices, which are rich in content. Markets—that is, actual choices by sellers and buyers—reveal and stimulate the discovery of knowledge that is otherwise left undiscovered. Market prices, free to fluctuate spontaneously, deliver that ever-changing knowledge sufficiently to permit effective economic calculation. To do their informative work, prices have to arise from real transactions. Without market prices (a redundancy, really) there would be no way to economize resources in behalf of consumer well-being. As Mises said, socialism, as an *economic* system, is impossible.

The existence of the Soviet Union did not refute Mises. After their disastrous postrevolutionary experience with War Communism (Trotsky recollected that the country looked into the "abyss") and the advent of Lenin's New Economic Policy, the Bolsheviks never again tried to abolish money, markets, and exchange. The government controlled most capital goods, but under the surface, markets—hampered to be sure—hummed. The West, moreover, was available for mimicking when necessary. Castro followed the Soviet model.

I am not saying Cuba has a free market. I'm saying it has an *unfree* market. That is far different from socialism, the obliteration of the market. Like the old Soviet Union, Cuba suffers from a government-saturated market. The state has clamped on so many regulations and taxes that the limits within which people can act are narrow. That is why Cuba is poor, lacking basic things we take for granted.

But within those constraints, the Cubans behave like entrepreneurs—buying low, selling high, profiteering, speculating, seeking at every turn to improve their circumstances. Despite what they may say, in their conduct Cubans are about as socialistic as Bill Gates and Warren Buffett. (See "Inventing Life in Cuba" by Marc Olshan, *The Freeman*, April 1998.)

Since Cuba has a government-saturated market economy, that makes it much more like the United States than Americans would like to think. It is interesting, then, that Castro invited President Clinton to try to persuade the Cuban people to give up "socialism." What could he (and most of his opponents) possibly say? Get rid of government-provided education and health care? End state-guided investment? He's *for* those things. The American people's economic activities are constrained by bureaucratic regulations, taxes, subsidies, and enticing "services" only to a lesser extent than the Cubans' are. The inane embargo on Cuban exports is one obvious example. Clinton and virtually everyone else in government enthusiastically support those restrictions. They want even more.

That's why the thought of the President trying to persuade the Cuban people to give up "socialism" is so funny. □

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THE FREEMAN
IDEAS ON LIBERTY

Statistics: A Vehicle for Collectivist Mischief

by John T. Wenders

Sir John Cowperthwaite served in Britain's administration of Hong Kong for over 25 years. From 1961 to 1971 he was Hong Kong's financial secretary, a position that gave him vast power over that colony's economic affairs. It was under his guidance that the theory of positive nonintervention was used to promote Hong Kong's astounding economic progress.

One of Sir John's crusades was to prevent the gathering of statistics on many aspects of Hong Kong's life. In Hong Kong, he said, "we are in the happy position where the leverage exercised by the government on the economy is so small that it is not necessary, nor even of any particular value, to have these figures available for the formulation of policy." For him, statistics were the tools of interventionists anxious to use the government to produce an outcome consistent with their collectivist view of society.

Amen.

The United States has taken a different route. The U.S. Constitution provides for the enumeration of citizens for the purpose of determining the number of each state's representatives in Congress. However, over the years, the Census Bureau has embarked on the collection of statistics far beyond those necessary for that purpose. We now gather data detailing every nook and cranny of our lives, thus providing fodder for the collectivist meddlers.

John Wenders is professor of economics at the University of Idaho.

Most of those statistics are simply synthetic. They force disparate things into an artificial whole that exists only in the mind of the synthesizer. The statistics are the lifeblood of those whose view of society submerges the individual in such groups as the poor, blacks, men, women, children, gays, senior citizens, to name a few. To the synthesizer, the individual has an identity only as he is a member of some collection of people.

For collectivists, not only is the individual identified by his group, but so is his behavior. Thus, we can no longer tell if one's behavior is good or bad, right or wrong, until we find out his group identity. And individuals are taught to test their behavior, not against any individual standard, but how it compares with what is socially—collectively—acceptable in their group. When someone's behavior does not measure up, it is society's fault, not his.

Similarly, class welfare is defined, from above, by the collectivized statistic without any reference to those who comprise the class. There is some higher measure of welfare that exists only in the eyes of the collectivist. In this world, the collective can be "better off" or "worse off" even if no individual in it is. Since income equality is "good" in the eyes of the collectivist, a society where everyone is equally poor is better than one where everyone is unequally richer. Any grouping of people, defined from above, is automatically better if minorities are represented at least proportionally. Individual

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human values are submerged for some collective, suprahuman measure of value that exists only in the mind of the collectivist. Suprahuman values are abstractions that have no meaning for individuals.

Statistics necessarily aggregate across individuals. These aggregates are, of course, the result of human action, but as aggregates they are not of human design. The unit of society is the individual, not the group. In aggregation individual action and choice are lost. The only groups that matter to individuals are those voluntarily joined. Any other group into which an individual is classified comes from the outside and exists only in the mind of the classifier.

Statistics that purport to describe groups say nothing about the causal mechanism that produced the data. In many cases, the observed statistic results from individuals each choosing what is best for them. If this is true, then the resulting statistic is an artifact that tells us nothing about the well-being of the individuals behind it. If the underlying decisions were all made by people doing what was best for them, then the outcome must be best from the perspective of those people. Synthetic statistics about the collective results are irrelevant.

Of course, even if the underlying process is right from each individual's perspective, collectivists will still claim that any statistics that show inequality or disproportionality prove that something is wrong. Beneath this claim is the implicit, but hotly denied, belief that people are all the same. The idea that people are different, and that statistical disparity merely reflects this, simply does not occur to the collectivists. These are the same people who celebrate multiculturalism and moral relativism.

The operational consequence of statistical collectivism is the demand for the state to deal collectively, and coercively, with the artificial problems suggested by these statistics. Differences become gaps: gaps in income, gaps in education, gaps in housing, gaps in health, gaps in other necessities. Problems are created and tackled from above by the collectivist mindset consumed with gapology. Leaving individuals and their associations alone is ruled out. Statistics fuel the interventionist engine.

One wonders what Sir John must be thinking now. □

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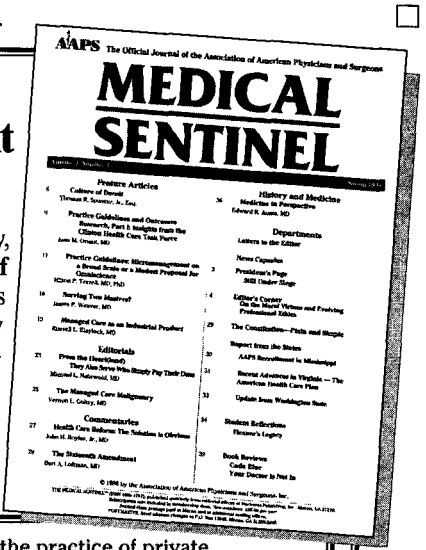
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Economics

The Power of Incentives

The surest way to get people to behave in desirable ways is to reward them for doing so—in other words provide them with incentives. This is so obvious that you might think it hardly deserves mention. But it does.

You might say that people shouldn't have to be rewarded (bribed) to do desirable things. Even when you acknowledge that incentives are necessary, it is not obvious how to establish the ones that motivate desirable action.

In one of my classes, I recently encountered the emotional resistance some people have to using incentives to accomplish good things. I was pointing out that the elephant populations in Zimbabwe and South Africa were expanding because policies there allow people to profit from maintaining elephant herds. A student who had stressed his environmental sensitivity responded that he would rather not see the elephant saved if the only way to do so was by relying on people's greed. In other words, he was willing to stand on principle as long as only the elephants suffered the consequences. His principle, one that I suspect was shared by others in the class, was that good things should be motivated by compassion and concern, not self-interest. I couldn't resist telling him that I would be impressed with his moral stance if, when he required delicate surgery to save his life, he refused to go to a surgeon and let his mother perform the operation instead.

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Convincing people that incentives are appropriate is not nearly as difficult as determining the appropriate incentives. Of course, we want incentives that motivate people to behave in desirable ways, but what is desirable? In some situations, the answer is rather obvious. But not always.

Every time you do a good thing, you necessarily reduce your ability to do something else good. This is an unavoidable implication of scarcity and is captured in the concept of opportunity cost, which I shall consider in more detail in a future column. There are always tradeoffs, and we often need information from many sources to know the best course of action. So the two important functions of incentives are: (1) to communicate information on the best things to do and (2) to motivate people to do them.

Incentives and the Treatment of Prisoners

In some cases the desirable course of action is clear, and these cases let us concentrate on the power of incentives to motivate people. The British government's practice of contracting with ship captains to transport prisoners to Australia in the 1860s provides a good example. The survival rate of the prisoners shipped to Australia was only 40 percent, which everyone knew was much too low. Humanitarian groups, the church, and governmental agencies appealed to the captains on moral grounds to improve the survival rate with more decent treatment. Despite these appeals,

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the survival rate remained at 40 percent.

Finally, an economist named Edwin Chadwick recommended a change in incentives. Instead of paying the captains a fee for each prisoner who walked onto the ship in England, Chadwick suggested paying them for each prisoner who walked off the ship in Australia. The improvement was immediate and dramatic. The survival rate increased to over 98 percent, as the captains now faced a strong incentive to protect the health of prisoners by reducing the number crowded into each ship and providing them with better food and hygiene in passage.[1]

Creating Incentives Directly and Indirectly

Desirable incentives can sometimes be created directly, as in the case of shipping prisoners. You know what you want done, so you create a reward (say, a cash payment) for doing it. Unfortunately, in most cases the type of behavior we desire requires subtly balancing competing objectives. In such cases, creating a direct incentive to do one thing can be *too* effective because it causes people to ignore other things.

The former Soviet Union was full of the perversities that can result from the direct application of incentives. Managers responded to incentives to increase the production of shoes, for example, by making only a few sizes, hardly caring which sizes best fit consumers. Such incentives affected people's behavior, but they failed to promote the social cooperation necessary for a productive economy.

When the objective is to motivate people to cooperate, desirable results can rarely be realized by directly establishing incentives. Instead, incentives have to be established indirectly through a set of general rules that allow them to emerge from social interaction.

Traffic demonstrates the importance of general rules in motivating cooperation. As aggravating as rush-hour traffic is, traffic flows reflect an amazing amount of spontaneous social cooperation. Without that cooperation, tens of thousands of commuters in every large city would get caught in a hopeless tangle of traffic. The basic rules that allow motorists to so effectively cooperate with one another are simple: (1) drive on the right side of the road; (2) go on green, either speed up or prepare to stop on yellow, and stop on red; (3) don't exceed the posted speed limit by more than ten miles per hour; and (4) don't touch. These rules convert our incentive to get to our destinations safely and conveniently into a pattern of accommodating behavior that serves the interests of all.[2]

The market economy is the ultimate example of how a set of rules can create a setting in which private incentives motivate social cooperation. Market economies don't create incentives directly. Indeed, in a literal sense, markets don't create incentives at all. The most important incentives come from the subjective desires of individuals: the incentive to find love, to earn respect, to make the world a better place, to provide for their families. Markets are the rules of conduct that harmonize these various incentives by making it possible for people to communicate their desires to others. The prices, profits, and losses commonly referred to as market incentives, are created by people's interacting with one another. These incentives, which can be communicated only through markets, contain information that promotes social cooperation. □

1. For more on this example, see Robert B. Ekelund, Jr., and Richard Ault, *Intermediate Microeconomics: Theory and Applications* (Lexington, Mass.: D.C. Heath and Company, 1995), pp. 21–22.

2. The example of traffic flow comes from Paul Heyne, *The Economic Way of Thinking*, 8th ed. (Upper Saddle River, N.J.: Prentice-Hall, Inc.), chapter 1.

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Should Government Build the Railroads?

by Burton Folsom, Jr.

On July 12, 1831, President Andrew Jackson, who was no prankster, did something that made many people laugh, some curse, and others rub their eyes in disbelief. He appointed 19-year-old Stevens T. Mason to be secretary and acting governor of the Michigan Territory.

Granted, Mason was a very intelligent teenager and his family was nationally prominent. But surely, his critics wondered, this was the worst case of political patronage ever seen. During the next ten years, however, the youthful Mason would often vindicate Jackson's judgment. Mason went from acting governor to elected governor. He plotted the strategy that brought Michigan into the Union, and he made deals that defined Michigan's boundaries on two peninsulas. Unfortunately, he also launched a gigantic scheme of state-run railroads and canals that almost bankrupted the state. As a result, Michigan voters went to the polls en masse to make their state a haven for free enterprise for the rest of the century.

The Mason story begins not in Michigan, but in New York, along a remarkable ditch that was dug in the 1820s. The Erie Canal, an astonishing achievement in engineering, had a big impact on American thinking. Here we had a canal 364 miles long that connected the Great Lakes with the Atlantic coast—and it was built not by entrepreneurs but by the state of New York. Suddenly New York City could trade with farms and cities throughout the midwest. Profits from tolls flowed into the state, and the whole Great Lakes region was open to settlement and trade.

Shortly after 1825, tens of thousands of New Yorkers and New Englanders filtered into Michigan via the Erie Canal. Governor Mason himself used the Erie Canal eagerly when he had to go to Washington to see President Jackson. Almost everyone in Michigan gushed with praise for this new canal, which brought them immigrants and took their exports. The message seemed obvious: states that want to get ahead need active governments to tax their citizens to build a transportation network.

To compete with New York, for example, Pennsylvania spent $14.6 million on its Main Line Canal from Philadelphia to Pittsburgh. Maryland and Massachusetts joined in the rush with a variety of state-supported projects. Illinois and Indiana began elaborate canal networks in 1837, just when Michigan entered the Union. This was when railroads were being built, and some states began to lay track and buy locomotives.

The State as Creator

To Mason this was all exhilarating. Maybe the traditional theory of limited government was wrong. Maybe states could be creators, at

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least in the area of transportation. And after all, it was state governments, not the one in Washington, that were building these canals.

Even as territorial governor, Mason urged Michigan to lay the foundation for the state to build internal improvements. When delegates met in 1835 to write the Michigan constitution, they—with Mason's encouragement—wrote the following into law:

> Internal improvements shall be encouraged by the government of this state; and it shall be the duty of the legislature, as soon as may be, to make provisions by law for ascertaining the proper objects of improvement, in relation to [roads], Canals, and navigable waters. . . .

In other words, Michigan's constitution almost required the state to fund internal improvements.

After this constitution was adopted, Mason publicly supported an activist state government. "The spirit and enterprise which has arisen among our citizens, if fostered and encouraged by the State, cannot fail to lead to lasting prosperity," Mason said. By 1837, three weeks before Michigan entered the Union, Mason was more urgent: "The period has arrived when Michigan can no longer, without detriment to her standing and importance as a state, delay the action necessary for the development of her vast resources and wealth." He was also optimistic: "we cannot fail soon to reach that high destiny which awaits us. I . . . demand immediate legislative action."

With Mason leading the cheers, the legislature met and almost unanimously passed an elaborate internal improvements bill. Democrats and Whigs alike joined in the public support for it. When the alternate strategy of private ownership came up, Mason recommended that the canals and railroads "should never be beyond at least the partial control of the state." "Extortion from the public" was what Mason called one bill to charter a private railroad. Most Michiganians seemed to agree. The Detroit *Daily Advertiser* noted that "Dewitt Clinton . . . built the [Erie] Canal with the funds of the state. What would be thought of the policy of surrendering that great work to the control of a private corporation[?]"

The example of the Erie Canal had become the ace that trumped all opposing arguments. And if one state subsidy was good, two must be better, and three better yet. Michiganians were so confident that state projects would flourish that they promised to build two railroads from Lake Erie to Lake Michigan, and a couple of major canals across the state as well.

Bad Luck, Bad Judgment

Mason thought the state should spend $5 million to build these projects. Actually, that was just start-up money. As soon as the anticipated tolls started pouring in—as happened with the Erie Canal—the state could then build more. The legislature approved the $5 million. Then the legislature authorized the governor to negotiate a $5 million loan with the lender of his choice under the best terms he could get, as long as he didn't exceed 5¼ percent. The state, in this arrangement, would issue bonds for the $5 million and pay them back as tolls came in from the railroads and canals.

Bad luck was the first problem to strike. The national economy went into a tailspin—the Panic of 1837—and capital was hard to borrow. Then came distractions. While in New York to talk with investors and study the bond market, Mason became sidetracked by Julia Phelps, the daughter of a wealthy leather merchant, Thaddeus Phelps. Mason courted and married her in 1838.

Then came bad judgment. Businesses were failing because of the panic, and most sound investors wanted more than 5¼ percent for their money. Mason finally persuaded the officers of the Morris Canal and Banking Company, a reputable firm, to buy the Michigan bonds. They promised to pay him the $5 million in regular $250,000 installments over several years. Mason gave them the bonds and went back to Michigan with their promise. The Morris Company turned most of the bonds over to the Pennsylvania Bank of the United States, which then sent them to Europe

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as collateral for its own investments. Within three years, both the Morris Company and the Pennsylvania Bank went broke, leaving Michigan with a $5 million debt scattered among European investors.

The Clinton-Kalamazoo Canal

An even greater disaster were the projects Michigan built. First was a canal that was to begin in Clinton Township near Detroit and extend 216 miles west to Kalamazoo. The Clinton-Kalamazoo Canal began with high hopes and much fanfare. Mason broke ground in Mt. Clemens in 1838 to celebrate the start of digging. Bands, parades, speeches, and a 13-gun salute commemorated the occasion. Then came reality. The Board of Internal Improvements, which Mason appointed to supervise the projects, hired different contractors for each mile of the canal, and these contractors each had different ideas on how to build a canal. One thing they all did wrong was to make the canal only 20 feet wide and four feet deep—too shallow for heavy freight and too narrow for easy passing.

After seven years and only 16 miles of digging, the ledger for the unfinished canal read: "Expenses $350,000, Toll Receipts $90.32." With funding scarce, the board decided sometime around 1843 to cut its losses, abandon the canal, and focus on the two railroads. When construction on the canal stopped, some workers went unpaid and they stole materials from the three locks on the canal. Soon even the completed parts of the canal were ruined.

The Michigan Central Railroad

The two railroads also had problems. The Michigan Central was to go from Detroit west through Ann Arbor, Jackson, and Kalamazoo and on to St. Joseph on Lake Michigan. Boats at St. Joseph could then take freight or passengers to Chicago and back. The route went through prosperous wheat farms and the state's larger cities, but poor construction and management of the road drained most of its profits each year. The Central was built with strap-iron rails, which consisted of thin strips of iron strapped onto wooden rails. These rails were too fragile to carry heavy loads. Rather than switch to the more expensive and durable T-rails, the Board of Internal Improvements chose to run regular heavy shipments over the existing tracks and repair them frequently. Not only was this practice dangerous, it was more costly to the state in the long run.

Robert Parks, who wrote a detailed book on Michigan's railroads, found a deplorable situation on the Central:

> [O]verloaded locomotives were run at twice the recommended safe speed. Under the strain of continuous operation and jarring impact of high speed on strap-iron rails, locomotives and cars were shaken to pieces, and the cost of operation mounted dramatically. Rails were broken and timbers crushed under the heavy loads bouncing over their surface.

By 1846, the Central had been extended only to Kalamazoo. It had technically been profitable each year, but did not earn enough to pay for needed repairs and new rails.

The Michigan Southern

The second railroad, the Michigan Southern, was to parallel the Central in the southern tier of counties from Monroe to New Buffalo. Financially, the Southern was a stunning failure. It had the same problem as the Central, with heavy loads on strap-iron rails. What's worse, the Southern was built poorly: the roadbed was shaky and the curves too sharp for locomotives. Monroe, on Lake Erie, proved to be too shallow a port for heavy freight to enter or exit. Also, the towns west of Monroe were too small to send much traffic on the Southern. By 1846, the road had only reached Hillsdale, about half-way across the state. It had cost over $1.2 million to build that far and its earnings were small. The road did little to move goods or people across the state; it drained capital that could have been used more wisely.

Michigan spent almost $4 million on the Clinton-Kalamazoo Canal, the Michigan Central, and the Michigan Southern. The state

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Stevens T. Mason

spent about $70,000 surveying the Michigan Northern Railroad, from Port Huron to Lake Michigan, before abandoning it. It also spent $47,000 clearing the route for a canal and turnpike near Saginaw. Officials soon quit the project, and the materials "either rotted or were expropriated by local residents."

Many of these problems occurred after Mason's terms as governor, but he received most of the blame because he had touted the projects and signed the loan. In 1837, he had narrowly won re-election, but in 1839 his Whig critics were loud and brutal. Mason chose not to seek a third term. By that year he had begun to consider if the problems with the projects were more than just bad luck or poor management. Maybe the state should never have drifted into economic development. In Mason's final address as governor, he said:

> [T]he error, if error there is, was the emanation of that false spirit of the age, which forced states, as well as individuals, to over-action and extended projects. If Michigan has overtasked her energies and resources, she stands not alone, but has fallen into that fatal policy, which has involved in almost unparalleled embarrassments so many of her sister states. Now, however, the period has arrived, when a corrective should be applied to the dangers which seem to surround her.

A "false spirit of the age," Mason said, may have moved states into the "fatal policy" of funding state projects. Michigan had too many railroads and canals and too few people to pay for them. But, as Mason had begun to realize, in a state-supported system this result would have been hard to avoid. The funding must come through the legislature, and the legislators naturally wanted projects in their districts. Jobs and markets were at stake. Some historians have suggested that if the Michigan Central had been the only project built, the strategy of state funding might have worked. But this was politically impossible. The legislators in the towns along the Central—Detroit, Ann Arbor, and Kalamazoo—needed votes from elsewhere to have their railroads built. The price for these votes was a commitment to build canals in Mt. Clemens and Saginaw and a railroad in Monroe and Hillsdale.

Political Manipulation

Mason actually saw this problem early and tried to stop it by centralizing power in the Board of Internal Improvements. The board's decisions, however, proved to be just as politically motivated as the legislature's. Many legislators pressured (and possibly bribed) members and some secretly made money from projects.

The story of Levi Humphrey is a case in point. Mason appointed Humphrey, a key Democrat in the state, to the board. When Humphrey took bids for constructing the Michigan Southern, he manipulated the results to assure that his friends in the firm of Cole and Clark won the contracts. Cole and Clark then charged three to four times the market price for supplies. When the complaints reached the legislature, Cole and Clark used some of their profits to bribe witnesses. The Whigs complained loudly, but when they won the governorship in 1839, they did not do

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much better. In 1840, the board overspent its budget and covered it by falsifying its records.

The problem was not just corruption; it was human nature. Officials did not spend state money as wisely as they would have spent their own. If Mason, for example, had been a wealthy industrialist, would he have invested $5 million of his own money with bankers he hardly knew during a national depression? Would any of the legislators have done so?

The spending policies of the board raise similar questions. In 1838, for example, it had a bridge built over the River Rouge. The problem was that the bridge they decided to build could not carry heavy freight. The Central, not the builders, lost almost $10,000 that year hauling passengers and freight around the bridge. Since no individual owned the bridge, no one had a direct financial stake in building it well—or even protecting it. The next year an arsonist destroyed the bridge.

In another example, the board ordered iron spikes for the Michigan Southern in 1841. The contractors, however, only put one spike in every other hole along the track. They stole the rest of the spikes and, when questioned, they persuaded the board that the unused spikes were defective. The board did not own the spikes or even have to ride on the rickety railroad that resulted; they simply believed the contractors and left the track partly unspiked.

The Boy Governor, no longer a boy, left office in 1840 at age 28. He had served almost nine years as secretary, acting governor, and elected governor. During this time, he had focused so intently on administration that he had left office almost penniless. He decided to leave Michigan for New York City, his wife's home, and make his fortune there in law and business. As he entered Buffalo and made his way across the Erie Canal to New York City, he may have wondered why the experiment with an active government worked so much better in New York than in Michigan. During the next two years, however, if Mason studied local politics, he saw New York repeat Michigan's experience. State legislators in districts outside the Erie Canal area had won eight new canal projects at a cost of $9.4 million. These new canals failed miserably and caused an economic collapse in the state, forcing eight banks to close and new taxes to be imposed.

Pennsylvanians did even worse. They spent $14.6 million on a risky canal from Philadelphia to Pittsburgh. The large losses on it each year helped force the state into default on its bonds. Several other states also defaulted on their internal improvement bonds, which damaged U.S. credit abroad and made Michigan look better. How much attention Mason paid to this we don't know. He died of scarlet fever on January 5, 1843, at age 31.

Mason was gone, but his "false spirit of the age" speech in 1840 had reopened the debate in Michigan on the role of the state in economic development. Right from the start, the government lost money building and operating the state's system of canals and railroads. William Woodbridge, the governor who followed Mason, first suggested selling the railroads to entrepreneurs and getting government out of the internal improvements business. At first, many resisted the idea. Legislators wanted railroads in their districts at taxpayer expense; they worried that entrepreneurs would build them elsewhere.

"The Errors of Our Policy . . ."

As the number of blunders on the projects began to multiply, however, more pressure came for the state to privatize. John Barry, who was elected governor after Woodbridge, echoed Mason and talked about "the spirit of the times unfortunately [becoming] the governing policy of states." Barry argued that "in extraordinary cases only . . . should a state undertake the construction of public works." He continued: "Seeing now the errors of our policy and the evils resulting from a departure from correct principle, let us with the least possible delay correct the one by a return to the other."

Thomas Cooley, Michigan's most prominent lawyer in the 1800s, observed firsthand the way the state ran its railroads. In a history of the state, he wrote, "Doubts were arising in the minds of the people whether the state had been wise in undertaking the construction and management" of internal improvements. "These doubts soon matured into a settled

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conviction that the management of railroads was in its nature essentially a private business, and ought to be in the hands of individuals. By common consent it came to be considered that the state in entering upon these works had made a serious mistake."

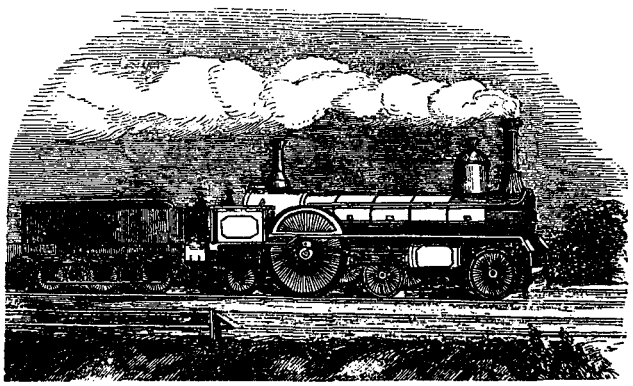
By 1846 Governor Alpheus Felch, who had followed Barry, carried the day for privatization. "The business of transporting passengers and freight by railroad is clearly not within the ordinary design of state government," Felch observed. The legislature finally agreed and voted to sell the state's public works in 1846. The state took bids and sold the Central for $2 million and the Southern for $500,000. As a result, Michigan recovered 90 percent of its investment in the Central and 44 percent in the Southern. If the losses on the canals and other projects are included, the state—through this sale—recaptured about 55 percent of its total investment in internal improvements. This decision helped the state cut its bureaucracy and also avoid bankruptcy.

As a condition of the sale, the new railroad owners had to agree to rebuild both lines with quality rails and extend them to Lake Michigan within three years. It had taken the state nine years to move the lines not much more than half-way across the state; the new entrepreneurs had to rebuild that part and complete the rest in just three years. When they did so, while keeping rates competitive, Michiganians knew they had learned something. They moved quickly to write this discovery into law.

A New Constitution

The next year, 1850, Michigan held a state constitutional convention. The proper role of government was one of the issues. The 1835 constitution, which mandated government support for internal improvements, was changed to include this: "The State shall not subscribe to or be interested in the stock of any company, association, or corporation." Further, "the state shall not be a party to or interested in any work of internal improvement, nor engaged in carrying on any such work" except for the donation of land.

The public debate that followed showed much support for the new constitution. "Looking at it as a whole," said the Grand Rapids *Enquirer*, "we honestly believe that if it had been adopted at the organization of our State Government, our State would now be out of debt, prosperous, and flourishing." In November 1850, the voters of Michigan overwhelmingly accepted the new constitution. Michigan had learned from its history. The building of railroads and the development of resources—lumber, copper, and chemicals—would be done by private enterprise. □



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THE FREEMAN
JUNE 1998

Great Turnabouts in Economics, Part II

"I used to love hedgehogs but those were 'my salad days when I was green in judgement'. Now I prefer foxes—Smith over Ricardo, Mill over Senior, Marshall over Walras."

—MARK BLAUG[1]

Last November, I reported on three economists who courageously reversed their published views. Now, I'd like to add a fourth: Mark Blaug. He is a prolific and intense writer, and most famous for his arduous textbook, *Economic Theory in Retrospect* (Cambridge University Press, 1997), now in its fifth edition. Blaug is primarily a historian of economic ideas and as such, he is, to borrow from Peter Drucker, a "bystander," an unbiased reporter and critic of economic ideas. And my, does Mark Blaug write with profundity and wit. His latest work, *Not Only an Economist: Recent Essays by Mark Blaug*, is one of the most delightful books I've read in a long time. I found myself making notes and exclamation points on practically every page.

As perhaps the most profound keeper of economic thought since Joseph Schumpeter, Blaug has made remarkable progress. His unrelenting search for truth has led him along the intellectual road from Karl Marx to Adam Smith, and even now shows increasing sympathy with Joseph Schumpeter, Friedrich Hayek, and the Austrian school.

Blaug's intellectual odyssey is curiously broad: like Whittaker Chambers, he started out a Marxist and a card-carrying member of the American Communist Party, then became disillusioned and betrayed. He flirted with Freud, but now recognizes Freudian psychology to be a "tissue of mumbo-jumbo." Regarding religion, Blaug "was brought up an orthodox Jew, achieved pantheism by the age of 12, agnosticism by the age of 15, and militant atheism by the age of 17."[2] He has shifted ground as frequently as he has transferred allegiance: born in the Netherlands, educated in the United States, and now a resident of Great Britain.

The Perversity of Ricardo, Marx, and Sraffa

Blaug's sojourn in economics is equally diverse. Leaving Marx, he became a convert to the British economist David Ricardo, wrote his Ph.D. dissertation on Ricardian economics, and even named his first son after him. But eventually he concluded that Ricardian economics is flawed and too formalistic. Blaug is especially disturbed by the development of a perverse version of Ricardian

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economics known as Sraffian economics. Sraffian economics is named after Piero Sraffa, author of the obscure theoretical work *Production of Commodities by Means of Commodities* (Cambridge University Press, 1960), which has highly influenced Marxists and post-Keynesians. Essentially, Sraffa uses a Ricardian model to claim that national output is completely independent of wages, prices, or consumer demand. Accordingly, governments can pursue their grandest redistributive schemes without damaging economic growth in the least.

In a scathing critique of *The New Palgrave Dictionary of Economics*, Blaug lambastes Sraffian economics as mathematically obtuse and irrelevant to the real world, and assails the editors for citing Marx and Sraffa "more frequently, indeed, much more frequently, than Adam Smith, Alfred Marshall, Leon Walras, Maynard Keynes, Kenneth Arrow, Milton Friedman, Paul Samuelson or whomever you care to name."[3]

Recently, Blaug has criticized modern economics for the "noxious influence" of Swiss economist Leon Walras in creating the "perfectly competitive general equilibrium model," or GE for short. Most of the textbook writers, including Paul Samuelson, are enamored with GE, because of its mathematical precision. For example, the perfect competition model focuses on the final end-state of competition, rather than the competitive process itself. Blaug labels perfect competition a "grossly misleading concept" that ignores the role of the entrepreneur. He urges economists to "rewrite the textbooks" and replace the current Walrasian GE model with the dynamic Austrian view of the competitive process.[4]

Blaug on Austrian Economics

Joseph Schumpeter, F.A. Hayek, and Israel Kirzner have been in the forefront of developing the Austrian view of competition. Blaug writes favorably about them all. Although belittling Mises's methodology ("cranky and idiosyncratic") and his business-cycle theory ("empty"), he grants Mises and Hayek "the better case" in the socialist calculation debate. He rates Schumpeter's *The Theory of Economic Development* (1911) one of the three most important books ever written by an economist. Ultimately he prefers Hayek: "In short, it is Hayek, not Mises, who deserves to be patron saint of Austrian economics."[5]

Incomplete Conversion

Blaug's conversion toward free-market capitalism is on the right track. He has gradually shifted toward Adam Smith and Hayek, though he is still enamored with John Maynard Keynes, who he says caused a "permanent revolution." Keynes divides the time line between Blaug's two biographical works, *Great Economists Before Keynes* and *Great Economists Since Keynes*. His current attitude is summed up as "capitalism tempered by Keynesian demand management and quasi-socialist welfarism."[6] Hopefully, that's not the final word on his economic philosophy.

One last note. Regarding Blaug's intolerance of religion, I'm reminded of G.K. Chesterton's response to H.G. Wells's atheism: "H.G. suffers from the disadvantage that if he's right he'll never know. He'll only know if he's wrong."[7] And the last thing that Mark Blaug wants to find out is that he is wrong. □

1. Mark Blaug, *Economic Theory in Retrospect*, 5th ed. (Cambridge University Press, 1997), preface. According to the Greek poet Archilochus (c. 680 B.C.), "The fox knows many things, but the hedgehog knows one great thing."
2. Mark Blaug, *Not Only an Economist: Recent Essays by Mark Blaug* (Edward Elgar, 1997), preface.
3. Mark Blaug, *Economics Through the Looking Glass: The Distorted Perspective of The New Palgrave Dictionary of Economics* (Institute of Economic Affairs, 1988), p. 15.
4. Mark Blaug, "Competition as an end-state and a process," *Not Only an Economist*, pp. 78–81.
5. Ibid., pp. 90–91.
6. Ibid., p. 9.
7. Quoted in Joseph Pearce, *Wisdom and Innocence: A Life of G. K. Chesterton* (Ignatius Press, 1996), p. 133.

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BOOKS

The Mainspring of Human Progress
by Henry Grady Weaver
Foundation for Economic Education • 1997
• 271 pages • $12.95 paperback

Reviewed by William H. Peterson

"There can be no progress except through the more effective use of our individual energies."

The emblazonment of this quotation on the front cover of the new edition of Henry Grady Weaver's classic is timely. For the thought gets to the heart of the Austrian concept of methodological individualism, a counterpoint to the Keynesian macroeconomic approach that requires national planners in Washington to manage our economy. That approach ignores the role of creative, risk-taking individuals who are the mainspring of human progress. They are the subject of this welcome book.

Henry Grady Weaver (1889–1949), a General Motors marketing executive who made the cover of *Time* in 1938, saw the role of the individual as central in American business. That role can be highly constructive, cautioned Weaver, only if two conditions are met—limited government and people who adhered to an ethical code. He hailed the concept of natural law and extolled the Founders' political structure because it "unleashed the creative energies of millions of men and women by leaving them free to work out their own affairs—not under the lash of coercive authority, but through voluntary cooperation and moral responsibility."

Weaver did his homework well in this historical examination of the ideas and people who built the American dream. This edition, with a two-page preface by FEE founder Leonard E. Read, features a new and most perceptive ten-page introduction by John Hood, president of the John Locke Foundation and author of *The Heroic Enterprise*. Hood notes the ongoing assault on the American business system, from the American historians' putdown of "robber barons" such as J.P. Morgan and John D. Rockefeller, to more contemporary putdowns of such supposedly representative entrepreneur-villains as TV's J.R. Ewing and Hollywood's Gordon Gekko. Hood applauds Weaver for setting the record of the American business system straight.

That record would not have been possible, Weaver argues, without the basic legal framework of private-property rights and tightly constrained government. Nor would it have been possible without a moral framework of respect for the rights of others. Freedom cannot be separated from personal accountability. The Ten Commandments and the biblical injunctions against covetousness, and to "love thy neighbor as thyself" go far to explain the triumph of laissez-faire capitalism. As Weaver wrote: "Your natural freedom—your control over your own life-energy—was born in you along with life itself. It is a part of life itself. No one can give it to you, nor can you give it to someone else. Nor can you hold any other person responsible for your acts. Control simply can't be separated from responsibility; control *is* responsibility."

There is a whiff of Hayek's spontaneous order idea here. Weaver came out strongly for "unplanned planning" as the secret of American economic success. Free men and women have the opportunity to live their lives, plan their own activity, work with one another, pursue their own happiness—all without any overriding forced authority of government. Unplanned planning worked.

But Weaver is writing about much more than just the United States. What makes this book so powerful is its historical sweep. Progress occurs whenever you have the ingredients previously mentioned. One of his most remarkable chapters is on the success of the Saracens, whose moral code and minimal government produced a prosperous and peaceful civilization while Europe suffered through the Dark Ages. Freedom has always and everywhere been the mainspring of human progress.

Weaver credits Frederic Bastiat for his free-market ideas and two equally remarkable

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women who also guided his thinking, Isabel Paterson, author of *The God of the Machine*, and Rose Wilder Lane, author of *The Discovery of Freedom*. This new edition stands proudly beside their works. □

William Peterson, an adjunct scholar at the Heritage Foundation, is the Distinguished Lundy Professor Emeritus of business philosophy at Campbell University in North Carolina.

Property Rights in the Defence of Nature

by Elizabeth Brubaker

Earthscan • 1995 • 328 pages with index • no price stated

Property Matters

by James V. DeLong

The Free Press • 1997 • 390 pages with index • $27.50

Property Rights: Understanding Government Takings and Environmental Regulation

by Nancie G. Marzulla and Roger J. Marzulla

Government Institutes • 1997 • 325 pages with index • $79.00

Reviewed by Bruce Yandle

It has now been almost three decades since the beginning of the federal environmental misadventure, a period that saw the rise of the regulatory state and the erosion of private-property rights. During this time, federal statutes, regulations, and centralized control have systematically replaced a diverse mix of decentralized common-law rules, state statutes, and local ordinances, along with customs and traditions that previously protected property rights. With the federal takeover, the rule of law, which is based on protection of property rights, was replaced by the rule of politics, which respects few property-rights boundaries.

Fueled by a combination of environmental hysteria, political opportunism, and efforts by some industries to raise rivals' costs and block competitive entry, the environmental juggernaut first provoked outcries from firms and municipalities that bore heavy environmental costs. Speaking indirectly for their customers, auto companies, steel producers, and a host of other manufacturers called for special relief, and in some cases got it. Municipalities and state governments asked for federal money to pay for mandated improvements; the money valves were opened. Until recently, hardly anything was heard from ordinary Americans—the farmers, ranchers, homebuilders, countless operators of small businesses, and just plain citizens who head off to work each day. Diverse and unorganized, these citizens hardly understood why some major manufacturers were so upset about environmental regulation. After all, protecting the environment made good sense, especially when someone else seemed to be footing the bill.

But as the environmental steamroller made its mark, ordinary Americans were pulled into the fray. For many of them, the issue was a simple one: their property rights were being taken by regulation. It was happening in the name of wetlands protection, saving endangered-species habitat, preserving historic corridors, and enhancing national landmarks situated near their homes.

Across the nation, many people came to realize that they were bearing the cost of providing public benefits, and contrary to the Constitution, they were not being compensated when their property was taken for public use. The resulting public outcry spawned hundreds of grassroots property-rights organizations, and eventually generated a struggle nationwide to protect private property.

Significant parts of this struggle are recounted in three important books. Elizabeth Brubaker's *Property Rights in Defence of Nature* addresses the Canadian experience and emphasizes the important role played by traditional private-property rights in protecting environmental quality. Brubaker's book focuses on the common law. But much more than a primer on nuisance and trespass, this highly readable and heavily documented volume convincingly demonstrates the power of common law—the law of the people—to protect envi-

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ronmental rights. Replete with case-law vignettes, the book shows how air and water pollution was countered by common-law rules, how defense of property rights in trout held by fishing clubs overcame the polluting tendencies of cities and industries, and how, in many cases, common-law remedies were harsher and the rules stricter than those that came with statutes and regulation.

James V. DeLong's *Property Matters*, which addresses the U.S. experience, provides a powerful companion volume to Brubaker's Canadian story. Writing in a style that is as entertaining as it is logical, DeLong offers countless short episodes to teach his lessons. He first offers some pointers on property rights and then examines the fundamental concern for and importance of property rights held by the nation's founders. Along the way, he introduces the ideas of John Locke and the legal synthesis provided by Blackstone. DeLong's examination of the record—what has actually been accomplished as opposed to what some politicians and environmentalists claim is being accomplished—destroys the myths associated with the Endangered Species Act and wetlands protection. In short, the rhetoric is great, but the record is dismal.

In the case of the Endangered Species Act, what might be an asset—a species that could be protected—becomes a liability when freedom to manage land is taken in the name of species protection. The wetlands story is even worse. No wetlands legislation has ever been enacted. Instead, a body of administrative law, with criminal sanctions, has emerged from the bureaucracy. DeLong explains that if the rules were enforced using the most expansive wetlands interpretation, 75 percent of the United States territory could become subject to Corps of Engineers dictates.

The Corps has encroached on the traditional rights of farmers, ranchers, and ordinary citizens who find their right to productive use of land taken by regulation. People building homes, constructing duck ponds, and plowing land find themselves in violation of rules, and in some cases sentenced to federal prisons. All this is happening, according to data cited by DeLong, while the amount of wetland is rising, not falling, as a result of wetland creation. DeLong carries the reader through issues involving land-use planning, zoning, artists' rights, Indian rights, and intellectual property, always building a strong case for private markets, property-rights enforcement, and the rule of law.

Nancie and Roger Marzulla, widely known for their leadership and their organization, Defenders of Property Rights, have provided a primer and more in their book, *Property Rights: Understanding Government Takings and Environmental Regulation.* Taking a constitutional approach, the Marzullas first define property, explain the fundamental social role played by property rights, and then quickly focus on a central question: What is a taking? The answer is developed in good lawyerly fashion so that the nonlawyer will understand and appreciate the complexities involved.

The Marzullas give a highly focused treatment of environmental regulation and devote separate chapters to wetlands and endangered-species regulation. Unlike DeLong, they delve deeply into case law on these topics and take a similar approach when addressing Superfund and land use and zoning. Their last few chapters address legal procedures, difficulties to be encountered when litigating takings cases, and what appears to be emerging on the property-rights legislation front. Appendices provide President Reagan's executive order on takings, which sought to rein in the regulators, as well as two recent and key Supreme Court decisions on takings, the *Dolan* and *Lucas* decisions.

Friends of liberty who study these highly readable volumes will be rewarded for the effort. □

Bruce Yandle is a professor of economics and legal studies at Clemson University.

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Makers and Takers: How Wealth and Progress Are Made and How They Are Taken Away or Prevented

by Edmund Contoski

American Liberty Publishers • 1997 • 464 pages • $24.95

Reviewed by Daniel Hager

Man is distinguished from the lower orders of animals because of the frontal and prefrontal lobes in his brain that foster thinking ahead and planning. Man becomes a maker, rejecting momentary gains for the adoption of long-range goals, while the lower animals are merely takers. Government, inherently an instrument of force and plunder, constitutes a regression to a lower state of being. If humans are to prosper and thrive, government must be kept in tight check, just as the Founding Fathers of the nation advocated.

In *Makers and Takers*, author Edmund Contoski offers a timely warning. While the philosophy of individualism promoted the nation's rapid advancement, America has now imperiled itself by turning toward collectivism. The political drive for "diversity" aims at social and economic equality, negating what Madison cited as "the diversity in the faculties of men." Contoski writes, "Equal rights, correctly speaking, mean only that men are entitled to equal protection against force, which means: the liberty to be *unequal* in every other respect. Any attempt by government to make men equal in any other respect necessarily violates their rights, their liberty." The implications of this attack on equality before the law gravely concern the author.

According to Contoski, democracy needs to be limited because it is based on the fallacy that "wisdom resides in the majority, . . . that wisdom is defined by popular opinion," in defiance of Newton's demonstration of "the universal nature of truth." He asks whether people would care to have a decision on proposed surgery submitted to a popular vote, concluding that "It would seem desirable to have as few decisions as possible determined by democratic vote." Alas, our trend runs in the opposite direction.

He takes issue with John F. Kennedy's idealistic appeal, "Ask . . . what you can do for your country." Claptrap, says Contoski, who offers a better alternative: "Ask what you can do for your*self*." The contrasting cases of John Fitch and Robert Fulton illustrate his point. Fitch developed the steamboat in 1785 and offered the invention to "the country" and various state legislatures, but was continually stymied by indifferent politicians. Two decades later, Fulton refined the concept, received a patent, and launched water transportation's Steam Age: "Hoping to reap profits for himself, Fulton did more for his country incidentally than Fitch did by intention and years of self-sacrificing perseverance."

But now big government has the upper hand, achieved through what Contoski terms the collectivists' "quiet conquest" of lower education and their domination of higher education, as well as most information media. Constant propagandizing makes it easy for government to expand through economic regulation. Contoski describes regulation as a form of coercion fueled by the alleged need to protect "the common good." Actually, it's a system in which "some people obtain material benefits by employing force against others."

The author devotes many pages to demolishing excuses for regulatory intrusion. For example, he cites Lawrence Reed's refutation in *The Freeman* (November 1994) of Upton Sinclair's truth-straining "exposé" of turn-of-the-century meatpacking houses that led to the 1906 Meat Inspection Act and notes that its legislative successor, the ineffectual Wholesome Meat Act of 1967, was similarly driven by distortions of the truth. He also quotes from Edith Efron's exhaustively documented and lamentably neglected *The Apocalyptics: Cancer and the Big Lie* to counter public hysteria about synthetic chemicals, and he disproves much more hokum.

The collectivists have indoctrinated enough generations of Americans that the nation's original guiding principles have been nearly expunged. Contoski is right on target in writing, "The sad fact is that most Americans have never really understood the American system. They were fortunate enough to have been born into it and benefited from it, but

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they didn't really understand it." Most of our citizens' thinking is so ingrained with statist assumptions that they cannot conceive of any alternative and thus fear freedom.

This hard-hitting book can break apart encrusted thought patterns. It refutes an enormous amount of statist disinformation and explains that people should not fear the makers—the capitalists who bring us prosperity—but instead worry about the takers who obstruct them. Read this superb book, then pass it along. □

Daniel Hager is senior research associate with Patrick Henry Associates in East Lansing, Michigan.

The Tyranny of Gun Control

edited by Jacob G. Hornberger and Richard M. Ebeling

The Future of Freedom Foundation • 1998 • 93 pages • $15.95 cloth; $9.95 paperback

Reviewed by George C. Leef

People are eternally prone to wishful thinking. It's usually harmless because pipe dreams aren't often turned into action in our private lives. When an individual knows he will bear the costs and suffer the consequences of some action, reality quickly intrudes and he asks, "Will this *really* produce the results I want? What will the costs *really* be?"

Politics, however, cuts the connection between individual action and consequences. Because "the government" takes the action and appears to bear the cost, most people don't ask those questions. Politicians, therefore, can get away with selling snake-oil remedies; they know that most voters are suckers for grandiose plans wrapped in good intentions. People *wish* for solutions to problems and rarely ponder whether the proposed plans will really work and what they will cost.

That is why they keep trying to alleviate poverty with welfare and minimum-wage laws. That is why they keep trying to improve health care through socialized medicine. And that is why they keep trying to make the country safer through gun control, the subject of this new volume from the Future of Freedom Foundation. Edited by FFF president Jacob Hornberger and Hillsdale College economics professor Richard Ebeling, the book brings together 14 essays calculated to get people to think about gun control the way they would think about a home do-it-yourself project: will it work and what will it cost?

When the subject of gun control comes up, the words "Second Amendment" are rarely far behind. Opponents of gun control argue that among its many costs is the trashing of yet another section of the Constitution. Gun-control advocates wave away that argument, claiming that it wasn't meant to guarantee an individual right to possess firearms. In one of the essays, "What the Second Amendment Means," *Freeman* editor Sheldon Richman annihilates their claim. Richman demonstrates that the pro-gun-control interpretation is utterly indefensible and closes the debate with this crusher: even if you believe that the Second Amendment protects only the government's "right" to have a militia, where else in the Constitution is there any enumerated power authorizing Congress to regulate or prohibit individual ownership of guns? There is no such grant of authority.

Another key gun-control issue is the question of its impact. Many people want so badly to reduce violence that they merely assume that gun control actually does so. This is wishful thinking at its most dangerous. Jarret Wollstein's essay, "Will You Be Safer If Guns Are Banned?" takes on this notion. Wollstein writes, "Paradoxically, although firearms do not increase crime and violence, gun control laws do. Throughout the United States, when strict gun-control laws are passed, crime and violence get worse." He proceeds to support his contention with evidence drawn from many different parts of the nation.

In another excellent essay, "The Assault Weapons Scam," James Bovard exposes the intellectual dishonesty in the anti-gun lobby's manufactured hysteria over "assault rifles." In politics, labels and perceptions are far more potent than reality. Knowing this, gun-control advocates invented the meaningless term *assault rifle*. The vagueness of the resulting statutes has given officials, as Bovard writes,

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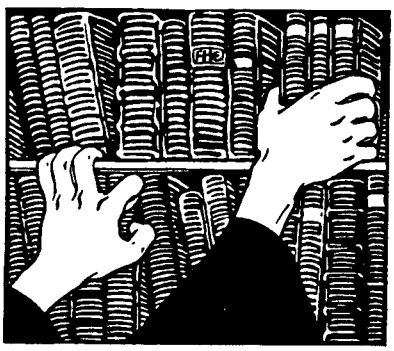
"arbitrary power to pick and choose which guns to ban and which gun owners to arrest and imprison." So-called assault rifles are virtually never used in crimes (and of course, the law won't do anything to prevent a determined criminal from getting and using one if he really wants to), but this episode has allowed a great expansion of government power over nonviolent gun owners.

Looking at history is often an antidote for wishful thinking, and Benedict LaRosa's splendid "Gun Control: A Historical Perspective" provides a potent tonic. Gun control (or, going back far into history as LaRosa does, weapons control) has been a favored policy of rulers who want a meek, compliant populace under their control. He includes an examination of Switzerland, where gun ownership is nearly universal. "The Swiss do not have an army—they are the army," one official Swiss publication proudly says. Despite the fact that Switzerland bristles with privately owned firearms of all kinds, gun-related violence is far lower there than in most nations with draconian gun laws.

This is just a sampling of the useful anti-gun-control material in this book. I only wish that there were more of it. An essay exploring why policies to *punish* wrongdoing are necessarily superior to policies intended to *prevent* it would have been a good addition. Still, if you want to be well armed in the battle against those who would prevent you from owning firearms, this is an excellent book to have around. □

George Leef is president of Patrick Henry Associates: Liberty Consultants in East Lansing, Michigan, and book review editor of The Freeman.



Rewarding Work: How to Restore Participation and Self-Support to Free Enterprise

by Edmund S. Phelps

Harvard University Press • 1997 • 198 pages • $24.95

Reviewed by Charles W. Baird

Economist Edmund Phelps proposes a new panacea for the troubles and pathologies of "disadvantaged" people in America—federal employment subsidies for low-wage workers. This book has delighted liberal interventionists, but I find it appalling.

Phelps begins by defining the "disadvantaged" as those in the bottom one-third income group. The subsidies he proposes would be credits against payroll and corporate tax liabilities for "qualified employers" who take on disadvantaged people for "eligible jobs." The credit would start at three dollars an hour for a worker whose "private productivity" is valued at four dollars an hour, and gradually decline at a decreasing rate to a $0.06 subsidy for a worker whose private productivity is valued at $12. He emphasizes that, unlike welfare, these subsidies could not be exploited by people who refuse employment.

Phelps asserts that his employment subsidies would "empower capitalism" by encouraging the "disadvantaged" to work, increase their self-esteem, and make them more self-supporting (hence the subtitle of the book). Once this happens there will be a greatly diminished role for welfare, since only the disabled would need it.

Phelps provides a justification for his subsidies based on the welfare economics of A.C. Pigou. He argues that a disadvantaged worker's "social productivity" is the sum of his "private productivity" and his "external productivity." Private productivity is "the productivity within the business." It is what the worker's labor services are worth to the employer. External productivity is the additional benefit enjoyed by society as a whole because of the worker's increased ability "to support [himself] and exercise responsibility as a citizen, community member, parent and

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spouse." A subsidy, "calibrated to the correct size," would supposedly internalize this "eternal productivity."

Such a scheme ignores all that we have learned from the public-choice school of political economy about government failure and from F.A. Hayek about the division of knowledge. Every government subsidy comes with increased government regulation. Just what is an "eligible job"? Who are the "qualified employers"? Is there to be yet another division of the Department of Labor charged with certifying jobs and employers? Phelps claims his plan would pay for itself through savings on welfare and crime. However, once such a scheme is put into place, interest groups like labor unions would advocate expansion of the subsidies, just as they have successfully done with the minimum-wage law. The subsidies would inevitably become just another increasingly costly feature of the welfare/transfer society.

Moreover, how can government calibrate the "correct" size of the subsidy for each worker in every job? Phelps's arbitrary sliding scale of subsidies would apply to all workers at all times and places irrespective of their unique circumstances. When we recognize that decisions will be based on politics, not economics, there is nothing left of the Phelps subsidies to recommend.

But there is much more to criticize about this book. For example, Phelps writes: "In acting through the government to pull up the rewards and thus to stimulate the participation and employment of low-wage workers, the more fortunate members of the labor force would be removing a source of some embarrassment. The more advantaged in society would gain pride and self-respect from having met their end of the social contract—of having acted justly. If so, they will be willing to pay something to achieve this satisfaction in the form of higher taxes."

He apparently believes successful people are merely lucky. In fact, of course, most successful people earned every penny they have by perfectly honorable means—voluntary exchange. They did well for themselves by providing opportunities to others. I can think of no better grounds for self-respect. It is apparently necessary to say one more time that if successful people really thought that they should help less successful people, they would do so. They don't need to wait for taxation to act.

Phelps also asserts that his subsidy scheme "fits the founders' conception of our government." He says that Jefferson's assertion in the Declaration of Independence of an inalienable right to the pursuit of happiness necessarily implies a right to a rewarding job. This is preposterous. To the founders, "rights" referred to a freedom of peaceful action that is prior to, and independent of, government. The founders' rights impose only a negative obligation on others to abstain from interfering. Government's principal job is to enforce those rights. Phelps's subsidies are positive "rights." They impose burdens on some to provide for others. The rights of those forced to pay conflict with the "rights" of those who are privileged to receive.

Perhaps the silliest claim in the book is Phelps's assertion that Keynes, along with Adam Smith and John Stuart Mill, was a "classical economic liberal." That says it all. □

Charles Baird is professor of economics and director of The Smith Center for Private Enterprise Studies at California State University, Hayward, and a Freeman *columnist.*

How Nations Grow Rich: The Case for Free Trade

by Melvyn Krauss

Oxford University Press • 1997 • 195 pages • $22.50

Reviewed by Daniel T. Griswold

Ever since the modern nation state emerged half a millennium ago, the question of how nations grow rich has been bound up with international trade. The battle line in the debate, from the time of the mercantilists and Adam Smith to the controversies today about GATT and NAFTA, has been whether nations grow rich by restricting free trade or by engaging in it.

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Professor Melvyn Krauss's new book, *How Nations Grow Rich: The Case for Free Trade*, won't end the debate, but it does provide a readable and well-argued defense of free trade on just about every point of current contention. As an emeritus professor of economics at New York University and the author of previous books on protectionism, foreign aid, and NATO, Krauss brings a deft hand to the task. Throughout his latest book, the author illuminates everything he surveys with clear writing and sound economic thinking.

Krauss begins at the beginning, by explaining the nearly two-century-old theory of comparative advantage in layman's language. The fundamental economic argument for free trade is that it allocates resources more efficiently by allowing people and nations to specialize in what they do best.

We don't trade with people in other nations to create more jobs. We trade to make ourselves better off. "Free trade does not create jobs—it creates income by reallocating or transferring jobs from the lower productivity to the higher productivity sectors of the economy. The argument for free trade—at least in the standard theory—is an efficient allocation of resources argument. Such reallocation increases income by increasing the average productivity of the nation's stock of productive resources," Krauss writes.

After his opening footwork, Krauss delivers a roundhouse right to the Clinton administration for its "managed trade" philosophy, followed by a series of quick jabs against the false arguments for protection. Among them is the assertion that free trade is only valid if it is "fair trade." "This argument—that equity demands the United States protect its producers when foreign countries protect theirs—has a certain appeal but is nonetheless fallacious. Free trade is fair trade to those whom it counts the most to be fair to—the domestic consumer," he writes. Other protectionist "tricks" Krauss exposes are the infant-industry argument, the "cheap labor" fallacy, and anti-dumping laws.

One of the most insightful sections of the book is Krauss's analysis of how the modern welfare state has corroded support for free trade. The tax bite and labor-market rigidity of the welfare state have created the high unemployment we see today in Western Europe, which in turn foments domestic pressure to curb imports in a misguided effort to save jobs. The welfare state's web of environmental and labor regulations that burden domestic producers invites further protection against rival industries in less regulated, and typically poorer, countries. Adding to the protectionist pressure are domestic subsidies to farming and other sectors, which then demand protection to maintain artificially high prices.

Krauss doubts that the welfare state and free trade can co-exist indefinitely. "The dilemma posed by this development is clear. Because of its evolving protectionism, the growth of the welfare state now threatens the very specialization and interdependence that is the basis for Western prosperity in the first place. The manner in which the Western industrial states resolve this dilemma to a large extent will determine their continued prosperity," he warns.

In the United States, the tension between domestic intervention and free trade can be seen in the effort to "export" our environmental regulations to other countries. Among the lobbying groups opposed to NAFTA and other trade initiatives are environmental groups who worry that competition with less developed nations will put downward pressure on U.S. environmental standards in a regulatory "race to the bottom." To placate the eco-protectionists, the Clinton administration wants to make the "harmonization" of regulations a part of any new trade agreements. Krauss argues that free trade need not lead to a lowering of environmental standards, but rather to a specialization of standards, with the more regulated countries expanding their low-polluting industries and other, less regulated countries expanding production of goods that produce relatively more pollution.

In the final three chapters, Krauss examines the wreckage of America's foreign aid programs, the demise of socialist planning, and the rise of regional trade agreements, including a critique of the European Union's drive for a single currency.

My only real complaint about *How Nations Grow Rich* is that Krauss did not write more

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of it. To be specific, his text is overstuffed with extended quotations, from the daily press as well as academic sources. It's fine to quote a few lines from Milton Friedman, as Krauss does to good effect in the section on anti-dumping laws. But the book would have been even more readable, and about 20 pages shorter, without the frequent quotes from the daily financial papers.

Even this complaint should be taken as a compliment to Melvyn Krauss. In *How Nations Grow Rich*, his own words are almost always sufficient to carry the argument in favor of the liberty to trade and invest with people beyond our borders. □

Daniel Griswold is associate director of the Center for Trade Policy Studies at the Cato Institute.

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LAW AND REVOLUTION:
The Formation of the Western Legal Tradition
by Harold J. Berman

"A magnificent volume, broad in scope and rich in detail; this may be the most important book on law in our generation."
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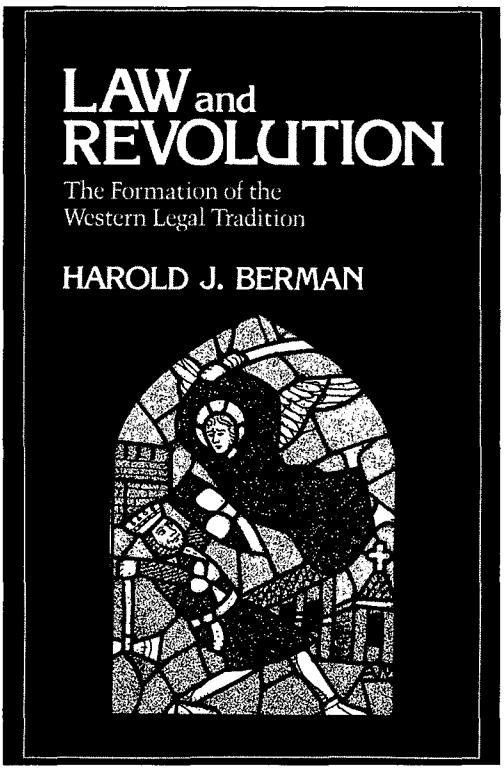

In this era of nation-states, we think of law as a body of rules that are centrally planned and imposed upon citizens by sovereign governments. Harold Berman's remarkable and award-winning book refutes this myth. Berman shows that law in the West is historically not the product of sovereign nation-states but, rather, of competition among different law-supplying institutions. Berman's research uncovers the exciting fact that during the law's formative era centuries ago, the crown competed with the church, with feudal manors, with cities, and with societies of merchants in supplying law. The lesson is profound: law generated by competing law-supplying institutions is likely to be superior to law produced monopolistically and centrally by a sovereign.

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CAPITAL LETTERS:

"In Defense of Misers"

To the Editor:

Since I work for an organization that studies philanthropy, I find Candace Allen and Dwight R. Lee's article ("In Defense of Markets and Misers," April 1998) interesting. I agree with their argument that Mr. M (the miser) provides a total benefit of $10 billion to others by hoarding his money, thus reducing the money supply and making goods more affordable. But I don't think they have shown that Mr. P (the big spender and philanthropist) "actually does less good than the unheralded contribution of Mr. M," that "Mr. M is actually providing more benefits to others," and that "misers provide benefits to others more effectively than do philanthropists."

I think that depends on whether Mr. P's philanthropy is wise or ill considered. To take two current examples, billionaire Ted Turner has pledged to give a billion dollars to the United Nations over the next ten years. Unfortunately, I think most of this money will have little effect and perhaps some negative effects (e.g., promoting dependency rather than economic growth in third-world countries by merely providing material assistance). But Bill Gates's pledge of $200 million to provide computers and Internet access to public libraries in low-income communities might have significant positive effects.

To take a hypothetical example: suppose a student becomes interested in biomedical research as a result of using these computers and the Internet. Suppose this interest might never have been sparked without these computers (the student becomes an accountant instead). The student goes on to study medicine in college and later discovers a relatively inexpensive cure for a major disease. In just the first few years after the cure is found, over $200 million is saved in health-care costs. While this example is probably not very likely, it is at least possible. Certainly other positive economic benefits of lesser magnitude are possible. Together, they may add up to well over $200 million—an amount that Bill Gates could just as easily put in a vault under his house.

In response to the authors' question, "which one of the two did more to benefit others?" I would say we don't know because we don't know what kind of philanthropist Mr. P is. In most cases, there is probably no way to measure the economic benefits that good philanthropists provide. But surely the spillover effects of philanthropy at least sometimes provide more in benefits than an equivalent amount of money kept in a vault.

Some of the authors' other remarks seem overgeneralized:

"Without the feedback of profit and loss, [nonprofits] don't know if they could be producing more value by using their resources in other ways." But certainly some nonprofits try allocating their resources to different programs and have the results of this measured by evaluation studies. These studies probably aren't as meaningful as profit-and-loss statements, but they do provide some useful information for making program improvements.

"Charities lack the incentive to direct resources to their most productive employment." Granted, it is better to rely on the profit motive to allocate resources than the goodwill of nonprofit executives, boards, and staff. But surely there are many people of goodwill in the nonprofit sector who seek to allocate resources efficiently and to avoid extravagant costs.

"Much of it [charitable contributions] goes into appeals for more contributions." I don't know if anyone has done a scientific survey, but fund-raising costs can vary from almost nothing to almost the entire budget of a nonprofit.

Dan Oliver
Research Associate
Capital Research Center
Washington, D.C.

Candace Allen and Dwight R. Lee respond:

All authors hope that their work will motivate thoughtful comments by thoughtful peo-

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ple, and so we were delighted to see the response to our article by Dan Oliver.

The main point of our paper is that markets and misers provide far more benefits than they are commonly credited with, because those benefits are widely dispersed and difficult to trace back to their origins. And indeed, we believe, and argued, that markets and misers accomplish more good than politics and philanthropists even though the benefits of the latter two are more appreciated because their benefits are concentrated and easily visible and traceable to their source. Thus, more good is accomplished indirectly through the market process than directly by either politicians or philanthropists, although of the two, we prefer the philanthropists.

Oliver's first concern with our paper is that we undervalue the potential benefits of philanthropists; the gifts of some philanthropists can have spillover effects that are greater than the "equivalent amount of money kept in a vault." There are no doubt cases in which this is true, as suggested by Oliver's hypothetical student who discovers the cure for a major disease because of a philanthropic gift. But our point was that the money kept in the vault lowers the price level a bit, which presents opportunities for people that can also have desirable spillover effects. These opportunities are easy to ignore because of the diffused nature of benefits created (exactly our point), but easy to appreciate once we consider the importance of marginal impacts. For example, there are millions of young people deciding whether to go to college, or take an additional course at the expense of less part-time work. Some of them will be on the margin of choice, and so the small per-capita increase in well-being provided by a miser can make a difference in how much education they get. Just as in the case of Oliver's student, some of "our" students can also go on to create enormous benefits because of the marginal impact of the miser.

Oliver agrees with us that the incentives of the marketplace do the best job directing resources into their most valuable uses, and we agree with him that "there are many people of goodwill in the nonprofit sector who seek to allocate resources efficiently and to avoid extravagant costs." But in terms of getting the job done, we feel that marketplace incentives trump the "goodwill in the nonprofit sector." We also agree with Oliver on the lack of "a scientific survey" backing up our claim that charitable organizations spend more on fund-raising activities than private firms spend on advertising. We have seen examples of extraordinarily large amounts of charitable revenues going back into fund-raising, and, for reasons discussed in our article, feel our claim is justified. But we recognize that this is ultimately an empirical issue.

We appreciate Oliver's comments. And we want to emphasize that our paper is in no way an argument against philanthropic activity. People should be free to do what they want with their money, including giving it to the United Nations. And, as opposed to Turner's gift, we are confident that much philanthropic activity is socially beneficial. But it's misers, not philanthropists, who need defense. By defending misers we aimed at making a broader point on the advantages we all realize from the dispersed and indirect benefits of the marketplace. □

(Candace Allen is a member of the affiliate economics faculty at the University of Southern Colorado. Dwight Lee, a contributing editor of The Freeman, *is Ramsey Professor of Economics and Private Enterprise at the University of Georgia.)*

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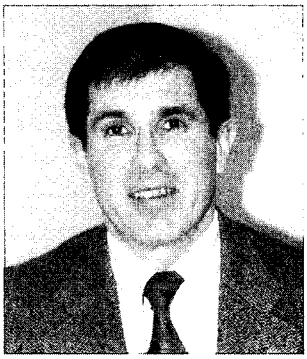

Cinema and the Capitalist Hero

The businessman has not fared well in film. Moviemakers have often attacked business and industry for destroying an old communal order based on equality and have lamented the businessman's preoccupation with material success and the dominance of large organizations in people's lives.

However, some films cast the businessman in a more favorable, even heroic, light by emphasizing the possibilities of life in a free society, the inherent ethical nature of capitalism and the businessman, and the strength and self-sufficiency of the hardworking entrepreneur.

The Heroic Corporate Raider

The corporate raider has been a tempting target for film makers, but not all movies portray this form of entrepreneurship as corrupt. In *Cash McCall* (1959), based on the 1955 novel by Cameron Hawley, James Garner plays a misunderstood tycoon and financier who is viewed by many as an unscrupulous robber baron who takes over companies, lays off employees, and sells the firms for large profits. McCall is actually a shrewd, productive, and efficient businessman who rebuilds acquired companies, operates them more effectively than their incumbent management, has high standards of personal and business ethics, and creates wealth without guilt. Commerce is depicted in the film as an honorable activity in a benevolent, life-affirming universe.

In *Other People's Money*, a 1991 film based on Jerry Sterner's play, Lawrence "Larry the Liquidator" Garfield, portrayed by Danny De Vito, wants to take over an outmoded, debt-free company that has a lot of cash. Larry plans to sell off the assets. The company's aging chairman, Andrew "Jorgy" Jorgenson (played by Gregory Peck), is a traditionalist and supporter of community values who doesn't want to see hundreds of people out of work. The climactic scene is a stockholders' meeting—a fight for control of the board of directors between Larry, who would make the stockholders money, liquidate the company, and shift the resources to better uses, and Jorgy, who would continue in a dying industry (copper wire). The film portrays Garfield heroically: he makes money for the stockholders—including retired people who aren't rich—while freeing resources to produce things that people want more than obsolete copper wire.

Both films accurately portray takeovers as nothing more than changes in ownership of assets, necessary for the efficient operation of a market economy.

The American Dream

Tucker: The Man and His Dream (1988), directed by Francis Ford Coppola, tells the true story of Preston Tucker (played by Jeff Bridges), a charming, persuasive, optimistic, innovative, and visionary maverick who chal-

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lenged the "Big Three" establishment by creating a utopian automobile. Tucker is portrayed as a Capraesque hero who fights the forces that eventually crush his dream. The film celebrates the American can-do spirit and the entrepreneur as the driving force of capitalism and wealth creation. According to the film, Tucker was the victim of Detroit and Washington, illustrating the need to separate economy and state.

An American Romance, a 1944 film directed by King Vidor, celebrates the American Dream by following its immigrant hero, Steve Dangos (played by Brian Donlevy), from his arrival at Ellis Island through his ascension from miner to steelworker to foreman to automobile entrepreneur who uses his knowledge of steel to build a safer, full-frame car. This film portrays America as the land of unlimited possibilities and views capitalism as the social system that best provides freedom and the opportunity to pursue one's vision of happiness.

Mac (1993) is the story of a hardworking Italian-American carpenter who realizes his dream of becoming a contractor. John Turturro plays Mac and directs the film of this uncompromising, honest, focused, and hardworking man with extremely high standards. For Mac there are only two ways to do a job, "the right way and my way and they're the same." The moral of the story is that each person has a God-given vocation and can contribute to the world by using his talents to the best of his ability.

Individualism and Independence

The Man in the White Suit (1952) stars Alec Guinness as Sidney Stratton, an entrepreneurial, visionary chemist who invents a fabric that will not wear out, stain, or become dirty. Leaders of both the textile mills and labor unions fear that the industry will be ruined and the laborers unemployed. Management and labor are guilty of thinking of only the immediate effects of the breakthrough on themselves as clothing makers; they do not consider that consumers will now have clothes and the other products that can be made with the newly freed-up resources. Although his fabric eventually falls apart due to a flaw in the formula, the heroic inventor is not discouraged. At the end of the film he is shown working to correct the error.

In *Sometimes a Great Notion* (1971, a k a *Never Give an Inch*), based on the novel by Ken Kesey, Henry Fonda plays Henry Stamper, the head of a small, independent, family-owned logging business in Oregon. Hank (Paul Newman), Henry's elder son, represents individualism and self-sufficiency. The hardworking Stampers are heroic businessmen who are anti-union, anti-socialist, and unamenable to anyone, including the government, who tries to tell them what to do. The family motto is, "Never give an inch." The unions strike the small company and other logging operations throughout the Northwest. The Stampers, who pride themselves on honoring their contracts, continue their operation despite union sabotage and violence.

Needed: More Pro-Capitalist Film Heroes

Films have depicted business people as over-materialistic, greedy, miserly, villainous, corrupt, unethical, hypocritical, insecure, insensitive, anti-culture, exploitative, smaller than life, repressed, and subservient to the establishment. Fortunately, some films, more than I have recounted here, have emphasized their heroic traits and accomplishments.

Cash McCall, Hank Stamper, Steve Dangos, and the cinematic Preston Tucker are great role models. Hollywood should give us others. □

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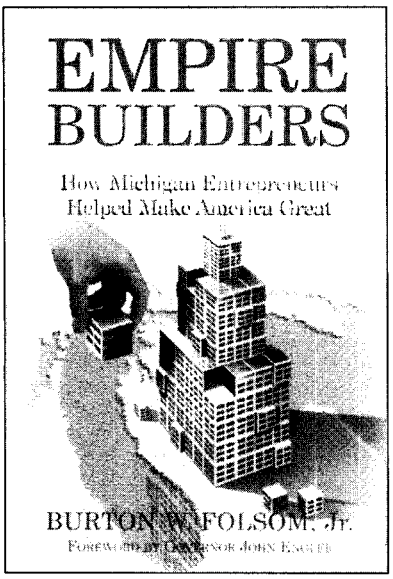
BY BURTON W. FOLSOM, JR.
Foreword by Michigan Governor John Engler

At a time when Americans seem confused about their past, *Empire Builders* inspires readers with triumphant heroes, dramatic stories, and a proud heritage.



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Michigan State University

Burton W. Folsom, Jr., is a senior fellow in economic education with the Mackinac Center for Public Policy in Midland, Michigan. He received his Ph.D. in history from the University of Pittsburgh and has taught American history at the University of Pittsburgh, University of Nebraska, Northwood University, and Murray State University, where he was a tenured full professor. He has written *Urban Capitalists* and *The Myth of the Robber Barons*. His articles have appeared in *The Wall Street Journal*, *The American Spectator*, *The Freeman*, *Human Events*, *Journal of Southern History*, and *Pacific Historical Review*.

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one cannot legislate the free market or create competition.
To have a free market the government must leave the markets alone;
to have the state make markets 'free' is again a contradiction in terms."

—D. T. ARMENTANO,
The Myths of Antitrust

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